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Politics this week

Feb 1st 2007
From The Economist print edition

Scores of **Iraqi** Shias were killed by Sunni insurgent bombs and mortars during the Shias' main religious festival, Ashura, while tit-for-tat killings in Baghdad and elsewhere continued. Earlier, near the Shias' holy city of Najaf, American and Iraqi troops fought an advancing force of a breakaway Shia sect, killing at least 260 of them. The newly appointed overall American commander of troops in Iraq said that "time was short" for turning things round. See article

In the first successful suicide-bombing for nine months inside **Israel**, a Palestinian from Gaza killed three people in a bakery located in a residential area in the Red Sea resort town of Eilat.

AP

At the African Union's annual summit in the Ethiopian capital, Addis Ababa, the president of **Chad**, Idriss Déby, denounced the president of **Sudan**, Omar al-Bashir, who failed in his attempt to win the organisation's chair for the coming year; it went instead to **Ghana's** president, John Kufuor. Mr Déby also assailed the AU itself for being "deaf and blind to ethnic cleansing" in Sudan's western region, Darfur, where the killing has spilled over into Chad.

Also at the AU summit, **Somalia's** interim president, Abdullahi Yusuf, agreed to hold a conference to try to reconcile his country's many rival clans. But no agreement was reached on sending an AU peacekeeping force to take the place of the Ethiopian troops who recently invaded the country to sweep Islamist militias from power.

As a token of **China's** growing interest in **Africa**, its president, Hu Jintao, began an eight-country, 12-day tour of the continent. Attention will be focused on his trip to Sudan where he will discuss international efforts to make peace in Darfur. See article

When's the Royal visit?

Nicolas Sarkozy, the centre-right candidate for the **French** presidency, made an election-campaign visit to London, where there are thought to be some 300,000 French residents. A poll showed Mr Sarkozy pulling ahead of the Socialists' candidate, Ségolène Royal. See article

Police in **Britain** arrested nine men suspected of planning to kidnap and murder a Muslim British soldier on leave from Afghanistan. See article

Germany ordered the arrest of 13 suspected CIA agents over the kidnapping, for five months, of a German national of Lebanese descent. Meanwhile, the foreign minister, Frank-Walter Steinmeier, was embarrassed by revelations that he had opposed the release of a German-born Turkish citizen held in Guantánamo Bay for four years. Investigators found no evidence of terrorist activity by the Turk, Murat Kurnaz. See article

Carla del Ponte, the United Nations war-crimes prosecutor at The Hague, urged the European Union not to resume talks with **Serbia** until it took steps to hand over Ratko Mladic, a Bosnian Serb general wanted for war crimes. The EU suspended talks last year in protest at Serbia's failure to arrest Mr Mladic.

Forcing one's hand

With threats of subpoenas hanging in the air, America's attorney-general, Alberto Gonzales, agreed to hand over classified documents about the government's (recently abandoned) **domestic spying** programme to a committee in Congress. Only selected legislators will be allowed to review the top-secret files.

Washington, DC, witnessed its biggest **anti-war rally** in a while. By some estimates around 100,000 people protested in the capital against George Bush's plan to send extra troops to Iraq. Meanwhile, a Senate committee held a hearing to confirm Admiral William Fallon as Mr Bush's top commander in the Middle East. The main topic of conversation

AFP

was Iran.

The former White House press secretary, Ari Fleischer, testified for the prosecution (under an immunity deal) at the trial of **Lewis "Scooter" Libby**. Mr Libby, a former chief of staff to Dick Cheney, has pleaded not guilty to charges that he obstructed an investigation into the leaking of a CIA officer's name to the press.

More bad news on **AIDS**. Trials of a vaginal microbicide called cellulose sulphate, which was intended to stop women becoming infected, were halted when it was found that those receiving the treatment were more susceptible to infection, rather than less so.

A shaming report

An official inquiry into hundreds of murders of opposition activists, priests and journalists in the **Philippines** concluded that the army killed most of them. But it rejected claims by human-rights groups that top military chiefs had sanctioned the murders.

Bangladesh's High Court ordered that elections in the country could not be held for three months, when it expects an overhaul of the election process to be completed. The country's election commissioners resigned as part of the reform process. An election scheduled for last month was postponed amid protests that the ballot would be rigged.

Six policemen and a civilian were killed by a roadside bomb in eastern **Sri Lanka**, the scene of recent fighting involving rebel Tamil groups.

Nepal's prime minister, Girija Prasad Koirala, pledged that the country would be a federal state in the future. Eight people have died in protests by southern Nepalese demanding the change over the past couple of weeks.

King Hugo

Venezuela's National Assembly granted powers to President Hugo Chávez to legislate by decree for the next 18 months. See article

Reuters

The first video images of **Fidel Castro**, Cuba's ailing president, released since October showed him looking stronger though still frail, and chatting with Venezuela's Mr Chávez. Mr Castro's health is a "state secret", but he is said to have suffered complications after intestinal surgery.

Canada's government said it would pay C$11.5m ($9.8m) to Maher Arar, a Canadian software engineer who was detained by American officials and flown to Syria where he was tortured. An inquiry found that Canadian officials had falsely told their American counterparts that Mr Arar was a terrorist.

Ecuador slipped towards mob rule. Thousands of protesters, organised by the new president, Rafael Correa, stormed the Congress, where a majority of newly elected legislators are opposed to plans for a constituent assembly.

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Business this week

Feb 1st 2007
From The Economist print edition

The **New York Stock Exchange** and the **Tokyo Stock Exchange** announced an alliance. The partnership covers trading-systems technology, investor services and regulation and is the latest expansive move into foreign markets by the NYSE, which is acquiring Euronext and recently took a stake in India's National Stock Exchange. For Japan's biggest stockmarket, the pact should help boost market confidence, which has been dented by a series of technical mishaps in its trading operations. See article

Citigroup agreed to buy **Egg**, an online bank, from Prudential, a British insurer, for £575m ($1.1 billion). Egg's sale price is much less than the £950m Prudential had said it was worth a year ago when Egg's minority shareholders were bought out. The bank made a loss of £145m last year, but Citigroup hopes that combining it with its own British consumer operations will prove a boon. See article

Deutsche Bank had a record year; its annual net profit rose by 70% to *euro*6 billion ($7.8 billion) in 2006, partly on the back of a resurgence in its investment banking business.

Climb every mountain

With $6 billion in development costs and a delay of some two years behind it, **Windows Vista** finally went on sale to consumers. Microsoft's latest operating system, its first since XP in 2001, has better security and new navigational designs. Bill Gates, the company's chairman, promised PC users that “the wow starts now”; analysts said they would sooner wait for Vista's sales figures.

Dell's chairman, Michael Dell, returned to his old job of chief executive after Kevin Rollins was dismissed. The computer-maker is trying to reboot its business in response to sliding market share and slowing growth. Investors were heartened by the news. See article

Google's fourth-quarter net income nearly tripled compared with a year earlier, to $1 billion (its annual profit for 2006 doubled to $3.1 billion). The company is prospering from website advertising revenue; the number of paid clicks rose by 61% in the quarter. However, Google's share price came under pressure after analysts cautioned its future profits might be hurt if it over-extended its new business.

US Airways withdrew its hostile $9.8 billion offer for **Delta Air Lines** after Delta's creditors threw their support behind the bankrupt carrier's reorganisation plan. Delta and its pilots' union insist the company has a future as an independent airline, but the bid has raised speculation about more attempts at consolidation in the industry.

The empire strikes back

India's **Tata Steel** beat Brazil's **CSN** in the bidding for Corus, an Anglo-Dutch steelmaker, so creating the world's fifth-largest steel company. Formed in 1999 from the remnants of British Steel, Corus is India's biggest foreign takeover. But Tata's share price fell sharply amid concern that the price it is paying, £6.2 billion ($12.2 billion), is too high.

US Steel said its annual net profit last year rose by more than 50%, to $1.4 billion. The company's European operations helped compensate for a rise in cheaper steel imports and falling demand from carmakers in America.

Altria made a long-awaited decision to spin off **Kraft Foods**. The idea was first mooted more than two years ago, but was delayed while Altria fought litigation about its Philip Morris tobacco business. Kraft's sales have been languishing of late, partly because of the trend towards healthier foods; the decision to divest the company will put an additional 1.5 billion of its shares in the market.

Ford reported an annual loss of $12.7 billion, its biggest ever, on January 25th. The carmaker is suffering from a persistent decline in sales and is busily restructuring itself. Meanwhile, **General Motors** said it would delay announcing its results because of accounting errors.

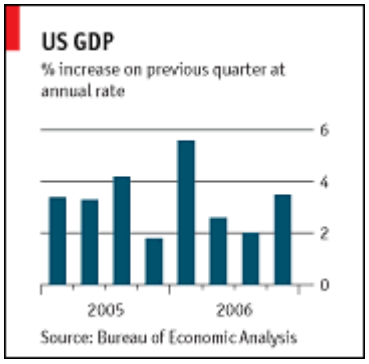
Manchester won the competition to host Britain's first Las Vegas-style **“super-casino”**. The city was chosen by the

independent Casino Advisory Panel over more high-profile bids, including one led by Philip Anschutz, an investor, for a casino at London's Millennium Dome.

Hank Paulson, America's treasury secretary, told the Senate Banking Committee that he would like eventually to see a “fully market-determined, floating **Chinese currency**”. The new Congress has made no secret of its irritation at China's stance on trade and exchange rates.

Shopaholics

America's GDP grew at an annualised rate of 3.5% in the fourth quarter, which was stronger than expected (the economy grew by 3.4% for the whole of 2006). A surge in consumer spending, helped by falling energy prices, boosted the figure. See article



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The world economy

India overheats

Feb 1st 2007
From The Economist print edition

India cannot run as fast as China without further reform

THE Indian tiger is on the prowl. This week, in an apt piece of symbolism, Tata Steel, which dates back to the days of the Raj, leapt into the league of top producers when it bought Britain's Corus, which includes the steelmaking remnants of the old imperial power. Nor is Tata alone: younger Indian companies such as Infosys and Wipro are storming international markets. Meanwhile, the world's business people and investors queue up to lavish money on India's talented engineers and computer scientists,

The roar from Delhi is echoing across Asia. After peevish years cast as China's underperforming neighbour, the huntress is now in hot pursuit. Over the past year the Indian economy has grown by an impressive 9.2%, not far behind China's 10.4%. At some point this year India's growth rate could even outpace China's; and if you measure things by purchasing power parity, India should soon overtake Japan and become the third-biggest economy, behind only America and China.

No wonder an increasing number of Indian businessmen, policymakers and economists are basking in the belief that their country is burning bright having at last broken free of its bureaucratic cage. An economy once famous for the "Hindu rate of growth", of 3% a year, was opened up by the reforms of the 1990s, many of them pushed through by the man who is now prime minister, Manmohan Singh. His government's latest five-year plan assumes that India can sustain average growth of 9%. Who can doubt "Incredible India", to borrow the slogan of its tourism campaign?

Tweaking the long tail

Fast growth is essential to pull millions of Indians out of poverty, so it is sad to pour cold water on this story. But that is precisely what is needed when there are so many alarming signs of overheating (see article). Across India prices are rising fast, factories are at full capacity, loans are piling up. Yes, the economic reforms of the early 1990s spurred competition, forced firms to become more productive and boosted India's trend—or sustainable—rate of growth. But the problem is that this new speed limit is almost certainly lower than the government's one. Historic data would suggest a figure not much above 7%—well below China's 9-10%.

When you mention overheating, many analysts point towards China. Yet India displays far more symptoms of the disease. Inflation has risen to 6-7% (compared with 2.8% in China); a record 99% of Indian firms report that they are operating above their optimal capacity; and credit is expanding at an annual rate of 30%, twice as fast as in China. Unlike China, India also has a widening current-account deficit—a classic sign of overheating, as domestic output fails to keep pace with surging demand. And if you are looking for a stockmarket bubble, Indian share prices have risen more than four-fold over the past four years, far more than in China. If something is not done, then a hard landing will become inevitable.

The Reserve Bank of India has been too timid in cooling down domestic demand: although one interest rate was

raised this week by a quarter point, the overall rise in rates over the past two and a half years has not even kept up with consumer-price inflation. But the main focus of the government's attention should be on supply—and dismantling the many barriers that keep its speed limit below China's.

So far, reform in India has focused on setting its inventive private sector free from the world's most fearsome bureaucracy. This has unleashed entrepreneurial talent, but more change is needed. Now is the time to tackle the public sector itself. Infrastructure, such as roads and power, and public services, such as education and drinking water, are woefully inadequate and limit growth. Even as the economy has been booming, many public services have worsened. It seems incongruous that somebody can own a mobile phone, yet has to waste hours queuing for drinking water. India's top computer scientists are feted around the world, yet most children in rural areas lack the basic education needed to find more productive work. Around half of all Indian women are illiterate, compared with a ratio of around one in seven in China.

Singh's songsheet

India's rulers have two bad excuses for not dealing with those roads, schools and hospitals. The first is theoretical. Many Indian economic commentators say that further structural reforms, though desirable, are not essential to keep the economy growing at 8% or more because of the “demographic dividend”. A fast-growing working population and a falling dependency rate (thanks to a lower birth rate) will ensure more workers, more saving and hence more investment.

India's demographic structure is indeed starting to look more like that in East Asia when its growth took off. But this mechanistic view of growth assumes that demography is destiny and that economic policies do not matter. In fact, open markets, education and investment, especially in infrastructure, were the three chief ingredients of East Asia's success. Population growth by itself does not add to prosperity, unless young people are educated and new jobs are created. India needs to reform its absurdly restrictive labour laws which hold back the expansion of manufacturing particularly.

The second excuse for doing nothing is practical: there is little room to spend more on schools and hospitals. India already has one of the biggest budget deficits among the large emerging economies (as much as 8% of GDP going by the widest measure). In fact, plenty can be achieved by reform, rather than just spending. Private investors are hesitant about putting money in infrastructure, because the regulators are not independent enough of populist politicians to guarantee a decent return.

If these things can be tackled, India can indeed match China's growth. Mr Singh remains a reformer, but his government relies on the support of the communist parties and, with today's prosperity, there is no stomach to take them on. The worry is that today's overheating will need to boil over before that mindset changes.

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The state of Britain

You've never had it so good

Feb 1st 2007
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Globalisation has done wonders for Britain, though not for all Britons

COUNTRIES, just like people, have moods; and Britain's is somewhat grumpy right now. It is bored and disillusioned with politicians, not least with Tony Blair. It is unimpressed by public services, despite the public money Mr Blair has poured into them. It is cross about rising taxes and interest rates. It is concerned about social cohesion and frightened by its home-grown bombers. It is furious about the Iraq war and George Bush. And, to cap it all, its cricket team can't win anything.

Yet in a way it is odd that Britain's spirits should be low. The place is enjoying a period of extraordinary prosperity. Fourteen years of stable growth have kept unemployment down. There have been social gains as well as economic ones: fewer children and pensioners live in poverty than ten years ago. Crime is broadly lower. And with prosperity has come renewed political clout. Britain has helped to shape aid for Africa, the debate on climate change, European enlargement and, last week, negotiations to restart world trade talks.

All this is especially remarkable in contrast with the recent past. A quarter-century ago, the home of the industrial revolution was closing factories and mines. The class war raged as unions took on the government and business. In the South Atlantic a weird little war palely recalled Britain's glory days. Comparison with mainland Europe is also gratifying. After the humiliation of *il sorpasso*, Britain's GDP per head has once more overtaken not just Italy's, but also France's and Germany's. Although Britons are too good-natured to indulge in anything as Teutonic as *Schadenfreude*, they might be forgiven for a small smirk at the troubles of their old rivals.

Hurrah for an imperial past

There are lots of reasons why Britain has done well, and most of them are connected to the country's enthusiastic embrace of globalisation (see survey). The early restructuring of its economy gave Britain an edge, accelerating the shift from mass manufacturing, where it had few advantages, to high-value-added goods and services, where it has many. A City that had earned its keep for centuries by financing trade and foreign investment attracted new business as others too began to think globally. Governments since Margaret Thatcher's have kept labour markets flexible and product markets competitive, allowing firms to respond nimbly to changing opportunities.

Perhaps because of its imperial and trading past, Britain is remarkably at ease with globalisation. While American politicians stoke anti-Chinese hysteria and French ones fuel worries about the disappearance of jobs to eastern Europe, British politicians keep off the subject. The last vestiges of Britain's home-owned car industry closed in the run-up to the last election in 2005, causing barely a ripple of protest.

But globalisation has social, as well as economic, consequences. The flow of foreigners into Britain has accelerated over the past ten years, partly because of demand (booming economies need new workers) and partly because of supply (developing-country disorder and new entrants into the European Union). Although this huge wave of immigration has done wonders for the economy, Britons have also found it socially troubling; and that's one of the

reasons why the country is not entirely at ease with itself.

Change usually makes people uncomfortable. So does the presence of lots of foreigners. But the government's policy has not helped. It chose long ago not to foist a common national identity on new citizens but to allow and indeed encourage them to retain the dress and language, faith and customs they came with. Time and propinquity, it was thought, would produce a richly diverse yet integrated society. But many now believe that multiculturalism has led instead to what Amartya Sen, an economist, calls “plural monoculturalism”—groups that live side by side but do not touch.

Policy, like custard, should be fine-grained not lumpy

This is of more than academic interest, for Britain harbours a pool of home-grown terrorists—a tiny minority of its 1.6m-strong Muslim community—who struck fatally once and may have been thwarted again this week (see article). A new survey for Policy Exchange, a think-tank, finds young British Muslims value symbols of their Muslim identity—the veil, for example, and *sharia* law—more than older ones and say they have less in common with non-Muslims than their parents do.

Should Britain then abandon multiculturalism and all its works and press for more assimilation? David Cameron, the leader of the opposition, thinks so, arguing that members of ethnic minorities need to be treated not as part of a community whose values they may not share but as individuals equal before the law. Mr Blair suggested something similar in December and Gordon Brown, chancellor of the exchequer and the prime minister's likely successor, is wont to wax lyrical on the importance of Britishness for all. The trouble is that Britishness is hard to define—especially since devolution has encouraged the Scots, Welsh and even English to prefer their more specific identities—and even harder to inculcate.

Yet the government should try to replace the lumpiness of multiculturalism with the finer-grained texture of individual rights and responsibilities. This is both truer to liberalism, which places the individual at the heart of things, and likelier to provide the economic flexibility that globalisation rewards. Such considerations do not lead easily to practical policies. But a start would include ditching the Downing Street guest-list of Muslim “community leaders”, rethinking faith schools, pushing to get more Muslim women into mosques and careers, and squelching the homophobes and extremists who refuse to acknowledge the right to free speech and equal treatment.

Much of that might be achieved by improving the quality of education, the best way to lift people out of ghettos into the mainstream. It is also, by neat coincidence, the key to ensuring Britain's success against ever-tougher competition as globalisation rolls on. No solution is perfect. Open your window, and, yes, you are bound to admit a few flies; but the main lesson of recent British history is that fresh air is good for you.

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African science

Amaizing grace

Feb 1st 2007
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Scientific research has a lot to give to Africa, and it is just starting to do so

Panos

ONCE upon a time, not so many centuries ago, there was a poor continent. Its name was Europe. Then it discovered three things: the free market, the rule of law and science-based technology. Now it is rich. A little simplistic perhaps, but the same thing happened in North America, with the same consequences, and it is now happening in Asia. What about Africa?

The need for the countries of Africa to embrace free markets and the rule of law gets written about ad nauseam, sometimes even allegedly by this newspaper. But the third leg of the stool is strangely neglected. Which is silly. For the lack of an indigenous base of science and technology will hamper Africa's development as surely as any stupid ideology or greedy dictator. Now, for the first time since their countries became independent, Africa's leaders are showing some interest in the topic. Better still, African researchers are starting to strike out on their own, addressing African questions from scratch, rather than trying to fit other people's answers to them.

How to culture a culture

Understandably, the most progress is being made in agriculture. Africa missed out on the Green Revolution that helped Asia on its way because, among other things, its soils often lack nutrients that Asian countries possess (it's a matter of the underlying geology of the two continents). That is now being addressed by the design of special fertilisers adapted to African soil. After a shaky start caused by the reluctance of European consumers to accept genetically modified imports, Africa is now embracing that technology, too. The first African-engineered crop to go on trial in the continent should be planted this year (see article). It is a form of maize that is resistant to a devastating virus. Maize, though an American crop originally, is one of Africa's most important foodstuffs.

Other crops are getting the once-over, as well. Uganda, for example, recently opened a laboratory dedicated to the scientific improvement of plantains, another important food crop. And South African scientists have developed, and Mauritanian ones deployed, a fungus that kills locusts by the swarmload (as a bonus, the dead swarms are a bonanza for local wildlife). African scientists, too, are developing a vaccine to stop sheep catching an infection that has put off Arab countries that used to be the main markets for African herders. Clearly, a small but impressive portfolio of scientific agriculture is starting to emerge.

Even the continent's politicians are starting to take notice. One or two, such as Paul Kagame, the president of Rwanda, have been long-term supporters of science, but for the first time in its history the African Union, meeting this week in Addis Ababa, put science and technology close to the top of the agenda. That is a double-edged sword, of course. If politicians are willing to cut the red tape that stops innovations spreading, and shake up the continent's sleepy government-run research institutes, well and good. If they start talking, as the African Union has, of “priority projects”, and drawing up lists that include space programmes, it might be time to run for the hills, or even the stars. And not all presidents are as wedded to the scientific method as Mr Kagame is. Thabo Mbeki, of South Africa,

still seems reluctant to accept the otherwise universal hypothesis that AIDS is caused by the human immunodeficiency virus—with all the dire medical consequences that flow from his refusal to take the right actions.

Still, Mr Mbeki will not remain in office for ever, and it is his comparatively rich country that is leading the charge. African science is still a young and fragile plant, but it is now being genetically modified to fit its environment. Let it grow.

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Kosovo

On the road to independence

Feb 1st 2007
From The Economist print edition

How America and Europe can make the inevitable acceptable to the Serbs

FOR the eight years since NATO aircraft bombed Slobodan Milosevic's Serbia into submission, the Serbian province of Kosovo has been in a state of suspended animation. Some 90% of its people are ethnic Albanians, almost all of them determined to achieve independence from Serbia. But for many people in Serbia the idea of Kosovo slipping formally away into independent statehood remains an anathema. And in the province itself some 17,000 NATO troops are still in place to preserve a grudging peace between the Albanian Kosovars and the remaining Serb minority.

Given the horrors that accompanied the break-up of Yugoslavia through the 1990s, it is understandable for outsiders to be wary of upsetting this precarious peace. One sign of how dangerous that could be was the outcome of last month's general election in Serbia. The greatest share of the vote was won by the Serbian Radical Party, which insists that Kosovo will remain an integral part of Serbia. Indeed, the Radicals' leader is an indicted war criminal awaiting trial in The Hague.

But the Kosovars are impatient, and their status cannot be left hanging forever. In 2005 the United Nations appointed Martti Ahtisaari, a former president of Finland, as its special envoy. Last week he presented his plan for the province's future to the six-nation “contact group” of America, Britain, France, Germany, Italy and Russia. This week he told the Serbs and Kosovars themselves what he has in mind. This is a form of supervised independence, similar to the status Bosnia was given in 1995. Ultimate authority for Kosovo would be transferred from the UN to a special representative of the “international community”, and Kosovo would be able to join international organisations.

This falls short of full independence. But for Serbia it may go too far. Although it softens the blow by promising autonomy to the Serb areas of Kosovo, and safety for Serb religious sites, it still offers a platform for Kosovo to declare independence and so will please no Serbian politician. Nor does it sit well with Russia, which has said that it will block in the UN Security Council any deal which does not have Serb approval. Nonetheless, it may yet succeed, with the right diplomacy.

Entice Serbia—and, if necessary, ignore Russia

One reason for optimism is that the position of the Radical Party inside Serbia is weaker than it looks. Kosovo was not the overriding issue in the recent election; corruption and economics probably swayed more votes. The Radicals, moreover, will not be the government. They collected fewer votes than the combined total of two other parties, the Democratic Party led by President Boris Tadic, and the Democratic Party of Serbia, led by the outgoing prime minister, Vojislav Kostunica. Both of these parties are well disposed to the European Union. Assuming that they form the government that will emerge from the horse-trading now under way, they are likely to have some understanding, albeit tacit and grudging, of the EU's determination to solve the Kosovo problem by supporting some form of independence.

The prospect of joining the EU is a carrot to dangle in front of Serbia as some compensation for the eventual loss of Kosovo. Last year the EU suspended talks on an association agreement—the first step towards membership—because of Serbia's failure to arrest Ratko Mladic, a Bosnian Serb general wanted for war crimes. If the Serbs renew their co-operation with the war-crimes tribunal, those talks should now resume—with the warning that their progress will be limited while Mr Mladic remains at large.

The Russians may be harder to entice. They argue mischievously that if Kosovo is allowed to become independent, so should South Ossetia and other pro-Russian enclaves in the Caucasus. And if Russia wants to, it can of course veto any UN resolution that sets Kosovo on the path to independence.

In that case Kosovo will have to go forward without the whole Security Council. Let America and European countries recognise an independent Kosovo, while the EU does what it can to calm the Serbs. Too much blood has been shed in the Balkans to allow prickly nationalists in Belgrade or muscle-flexers in Moscow to block progress towards a

stable future.

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About sponsorship

The Middle East

Where moderates fear to tread

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From The Economist print edition

Bolstering the forces of moderation doesn't mean just bludgeoning the extremists

AP

JUST about the only thing that everyone can agree on in the Middle East is that the region has rarely, if ever, been in such a mess. At least four bloody crises are crowding in on each other, none with an easy path to resolution. In Israel-Palestine, there has been no progress towards peace in six years. A discordant Lebanon is in danger of being torn apart all over again. Iraq's mayhem continues unabated. And Iran's Holocaust-denying president seems hellbent on acquiring a nuclear weapon that would not just threaten Israel's existence but terrify his Arab neighbours and provoke a nuclear arms race across the region. Indeed, the Sunnis of the Arab world are becoming increasingly twitchy about what they perceive as a rising Shia challenge, by Arab Shias in Iraq as well as by Persians, to their long-time hegemony (see article). No wonder that “moderate” (or at least pro-Western) forces in the region, the most active of them being Egypt, Jordan and Saudi Arabia, are desperate for their Western friends to help calm things down.

Everyone knows that solving the Israeli-Palestinian conundrum would massively help the West and its fearful local friends in their efforts to help the forces of moderation and modernity overcome those of fanaticism and backwardness. Yet on the face of things the omens for another push for peace between Israel and the Palestinians are poor. The Palestinians, now engaged in a furious factional war of their own, have a government only in name, while Israel's own domestic malaise has rendered its administration almost equally feeble (see article); both lots of people doomed to share the Holy Land are unusually short of leaders with courage or vision.

But at least they may be realising that things cannot go on like this. The longer there is no solution, the greater the risk that the lunatic fringe, abetted by the likes of Iran's president, may one day manage to drop a bomb on the Jewish state. Meanwhile the Palestinians' chaos and misery threaten to destroy what is left of the fabric of their society, leaving the husk of it to the extremists. Hence, in the past week or so, the insistence, by such well-meaning luminaries as Jordan's king and the Saudi foreign minister, that the time is ripe for negotiation.

The so-called Quartet—the United Nations, the United States, the European Union and Russia—are shortly to meet after being inert for too long. There is talk of skipping the step-by-step slog laid out in the tattered “road map” towards creating a proper Palestinian state alongside a secure Israel, and of going straight to “final status” talks. Israel's prime minister, it is suggested, should offer the Palestinians a firmer promise of a genuine state, while the Americans may re-engage as an active broker after years, under George Bush, of keeping their hands off—which meant giving Israel a free hand. The American secretary of state, Condoleezza Rice, who has so far done little to crack the whip for peace, has offered, at long last, to enter the fray as ringmistress for the first act.

Big caveats are in order. Helping the Palestinian president, Mahmoud Abbas, and his Fatah party simply to hammer the Islamists of Hamas is not the way to go. It is still better to seek a unity government that would cajole the relative pragmatists in Hamas (yes, they do exist) into accepting the reality of Israel and, of course, into disavowing violence, even if at first they agree only to a truce.

Don't forget the cedars either

Israel may be able to help break the logjam in Lebanon too. Hizbullah, the Shia Islamist movement seeking to overthrow Lebanon's beleaguered pro-Western government, cannot just be whacked into submission, any more than Hamas can—as Israel discovered during its ill-judged war last year. But Israel could wrong-foot Hizbullah by offering to vacate the Shebaa Farms, a patch of land taken by Israel during the war of 1967 and claimed both by Syria and Lebanon. An Israeli exit from Shebaa would remove the pretext under which Hizbullah says it must remain armed to the teeth in defiance of the UN—and which is a bone of contention with the Lebanese government. Israel should then try to draw Syria itself, however malign it has been, into the equation, with the Israeli-occupied Golan Heights as the main price of a peace treaty with Israel.

Even if Israel, the Palestinians, Lebanon and Syria were to start horse-trading in earnest, that would still leave the more intractable problems of Iraq and Iran. If a settlement were achieved in the Israeli orbit, it would not bring peace to the rest of the Middle East; too often, the Israeli-Palestinian stalemate is blamed for woes elsewhere. But it would be a great start. There is no time to lose.

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About sponsorship

Sudan and China

Mr Hu's mission to Khartoum

Feb 1st 2007
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Why China should insist on UN peacekeepers for Darfur

Alamy

HU JINTAO, China's president, is a seasoned traveller. At present he is on an eight-nation tour of Africa, a continent he knows well from two previous trips. He has every reason to expect a warm welcome. All over Africa a commodity-hungry China is winning friends by building roads, ports and railways. He will be especially welcomed this weekend in Sudan. For China not only buys about 80% of the oil exports that are making parts of Sudan rich. It also shields Sudan from being held to account in the UN Security Council for one of the largest atrocities of recent times: the killing of some 300,000 people and the uprooting of more than 2m in Darfur.

Omar al-Bashir, Sudan's president, will lay on a special tour of the sights in Khartoum. Mr Hu will see a booming city, awash in oil earnings. It is easy in the capital to get the impression that Sudan is a peaceful country forging a brave new future as a financial-services hub. All very Shanghai.

The truth is very different. As Khartoum booms, Darfur bleeds to death. The killing and displacement in the western region have not stopped just because they have slipped away from the headlines. If anything, matters have got worse—so bad in fact that the humanitarian agencies trying to provide for the millions of hungry refugees in the region have spoken up. For a long time the agencies have had to bite their tongues. The Sudanese government expels those who voice even the mildest criticism. Now they reckon they have little left to lose. This week six of the big charities issued a joint warning that their efforts would soon be “paralysed” by violence that is “worse than it's ever been”. In other words, the humanitarian lifeline is on the verge of snapping.

The government in Khartoum is not the only villain in the conflict. Darfur's rebel groups have contributed to the tragedy. But the Sudanese government is unquestionably to blame for preventing a solution. Its duplicity and evasions are endless. At the end of last year hope flickered briefly to life with an apparent agreement on the deployment of UN peacekeeping troops to bolster the small and overstretched force from the African Union (AU). The government in Khartoum accepted a ceasefire to allow the rebel groups to discuss new peace terms. Now February has come and Mr Bashir is still haggling over the shape and size of any UN force. A fortnight ago the Sudanese armed forces bombed the area where it thought the rebel meeting was going to take place. Neither appeals from the AU, nor the intervention of Ban Ki-moon, the UN's new secretary-general, have been able to budge Mr Bashir.

Might Mr Hu succeed where others have failed? He should certainly try. In many ways China's growing involvement in Africa has been good for all. In exchange for the oil and raw materials that are fuelling its economic rise, China has been building up Africa's neglected infrastructure. One thing that has added to China's popularity throughout the continent is that, unlike the Western helpers who append a miscellany of irksome conditions, the Chinese say they will not interfere in Africa's politics. In the case of Darfur, however, this liberal Chinese stance is being exploited as a licence to kill. There may be profit to China in turning a blind eye to all of this, but there is no honour. And in time the profit may dry up as well.

Invest in the future, too

That is because the fighting in Darfur is not just a humanitarian disaster that should rend the conscience of the world (though it should). It is also a threat to the newly established peace in the south of the country, and therefore to Sudan's future as a dependable supplier of oil and other commodities both to China and to the wider world. As it happens, most of Sudan's best oilfields are in disputed areas between the north and the south. As China's economic interests and dependencies spread, it is going to have to learn the need to invest in peace as well as pipelines. Sometimes that will require it to put unwelcome pressure on its trading partners.

Right now, Chinese pressure on Sudan could make all the difference to the prospects of inserting UN peacekeepers into Darfur. Such pressure will not be welcome in Khartoum. But the rest of Africa is repelled by the slaughter of Darfuris and by the circles Mr Bashir has run round the UN and the African Union. In Khartoum Mr Hu has a rare

opportunity to combine self-interest with statesmanship. He should grab it.

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About sponsorship

On Russian energy, Lord Kalms, idleness, American history, the brain

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Cut out the middle men

SIR – I agree that a few lessons need to be learnt from the dispute between Russia and Belarus over energy ("Loveless brothers", January 13th). The biggest lesson is that Russia wants to sell its gas at market prices to all consumers, irrespective of their political relations with Russia. This is a business issue and should not be politicised, for instance by suggesting that Russia is punishing its "former vassals".

The lessons for east Europeans are: learn to live without Russian subsidies, and don't blackmail Russia with threats of disruption to Russian energy supplies. The best way to stop these threats is to route energy directly from Russia to Europe. For example, Nord Stream will eventually pipe gas from Russia to Germany beneath the Baltic Sea. Projects like this should be supported as they benefit energy stability; eliminating the intermediaries between suppliers and consumers is normal business practice after all.

Vasily Kuznetsov
London

Lord Kalms

SIR – I refer to the article entitled "UKIP if you want to" in the Bagehot section of the 20th January 2007 edition. You state in your article that David Cameron has been "pushing [me] and [my] chequebook" away from the Tory Party and towards UKIP. The article goes on to say that Mr Cameron need not worry about "the blackmail of former donors", again a reference to me.

I have been a leading Eurosceptic for many years. I have not, however, made any donations to the Conservative Party for some considerable time, aside from modest contributions towards the campaign costs of individual Tory candidates. I am in no position to threaten to withhold funding in an attempt to influence Mr Cameron's policies nor, contrary to what is said in your article, have I suggested that I might do so. Your use of the word "blackmail" in this context is factually inaccurate and, I am sorry to say, offensive. I had hoped that *The Economist* could be trusted not to overlook facts in favour of journalistic colour.

Lord Kalms
London

Theatre critic

SIR – The Georgians and the Edwardians were not the first to condemn new forms of entertainment as morally reprehensible ("Don't shoot the messenger", January 20th). In his "Policraticus" of 1159, John of Salisbury lamented the lives of those who filled their time enjoying actors, mimics and jugglers, for

> "actors give [idleness] new life. Tedium steals upon unoccupied minds and they are not able to endure their own company unless they are pampered by the solace of some pleasure. Therefore spectacles and the countless hosts of vanities by which they who cannot endure to be entirely idle are occupied, but to their greater harm. Better it had been for them to have idled away their time than to have busied themselves to their own ruin."

Woe to the billion or so of us who will soon be tuning in to watch the Oscars.

Caz Zyvatkauskas
Toronto

Winners get to write history

SIR – Lexington's comment that the American revolution “got rid of feudalism” is bizarre (January 13th). Did he mean to describe the Britain of 1776 against whom the American colonists revolted? The parliamentary democracy where Adam Smith was publishing “The Wealth of Nations”? Most historians agree that it was precisely the absence of feudalism during the period that helps explain the start of the Industrial Revolution. Yet American mythology about 1776 portrays Britain as a cross between a Renaissance autocracy and Nazi Germany, rather than as the country that bestowed upon America the legacies of personal freedom, the rule of law and capitalism.

Andrew Porter
Wirral, Merseyside

Brainiacs

SIR – Your survey of the brain captured the complexities of current thinking about consciousness (December 23rd). One of the greatest challenges confronting research into consciousness is to define what it is. But not only do we not know what it is, we don't even know who, or what, is conscious. Is a cat conscious? A worm? A thermostat? My boss? And even if we were able to settle upon an acceptable definition of consciousness, we really have no idea how to study the problem.

This conundrum is a philosophical dilemma. Can consciousness be studied using a reductionist approach, or is consciousness an emergent property arising from brain complexity and thus not amenable to the divide-and-conquer approaches of reductionism? Conceptually, reductionism is the greatest triumph of modern science, enabling multifaceted problems to be reduced to their constituent molecules. Such thinking permits the design of drug molecules to treat complex human diseases or to modify other difficult biological disorders.

However, if we are unable to reduce consciousness to simpler building blocks or concepts, it may be impossible to apply the tried and true tools of modern science to the daunting task of understanding consciousness. Although some people (like me) are passionate reductionists, others believe this is a path doomed to failure when it comes to trying to comprehend “why I think” and “why I am”.

Donald Weaver
Professor
Departments of medicine (neurology), chemistry and biomedical engineering
Dalhousie University
Halifax, Canada

SIR – You missed the point regarding opposing sides in the nature versus nurture debate. The key difference is not between genetically determined and culturally determined views of human behaviour. Rather, it is about how biological and social scientists should contribute to the improvement of human well-being. Those who try to do so through physiological research look for a technical solution to suffering in an adjustment of the brain's neuro-mechanics. Those who try to improve well-being through social research find political solutions requiring adjustments in social relations.

Gregory Feldman
Assistant professor of international migration
University of British Columbia
Vancouver

SIR – With regards to criminals, your argument that without free will “the idea of responsibility for one's actions flies out of the window” is spurious (“Free to choose?”, December 23rd). On the contrary, if people respond deterministically to their environment, all the more reason to pass laws and hold violators accountable. In any case, the reduction of the brain to a mechanistic process does not necessarily add anything to the debate on responsibility. As David Hume would have it, either our actions are determined, in which case we are not responsible for them, or they are the result of random events, in which case we are not responsible for them.

Julian Reif
Washington, DC

SIR – I think Isaac Bashevis Singer should have the last word: “We must believe in free will. We've got no choice”.

Gabriel Guiloff
Santiago, Chile

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About sponsorship

Religion in China

When opium can be benign

Feb 1st 2007 | BEIJING, DONGLU AND HONGLIUTAN
From The Economist print edition

James Miles

China's Communist Party, reconsidering Marx's words, is starting to wonder whether there might not be a use for religion after all

Get article background

“DEVELOP the dragon spirit; establish a dragon culture,” urge large green characters at the high school in Hongliutan, a poor village at the foot of a range of bleak loess hills. Though dragon can be a synonym for China, it is a god known as the Black Dragon that is being invoked here. Without funds from the Black Dragon's hillside temple, in a gully behind the village, the school would not exist. Nor, most likely, would the adjacent primary school and the irrigation system that brings water from the nearby Wuding River to the village's maize and cabbage fields.

Many local governments in rural China are mired in debt. Recent central government efforts to keep peasants happy by abolishing centuries-old taxes have not made life any easier for these bureaucracies. With their revenues cut, rural authorities have found it ever more difficult to scrape together money for health care and education. So they are only too happy to allow others to share the burden of providing these services—even the Black Dragon, whose 500-year-old temple was demolished by Maoist radicals during the Cultural Revolution in the 1960s. Now officials in Yulin, the prefecture to which Hongliutan belongs, give the temple their blessing.

The revival of the Black Dragon Temple's fortunes is part of a resurgence of religious or quasi-religious activity across China that—notwithstanding occasional crackdowns—is transforming the social and political landscape of many parts of the countryside. Religion is also attracting many people in the cities, where the party's atheist ideology has traditionally held stronger sway.

The resurgence encompasses ancient folk religions and ancestor worship, along with the organised religions of Buddhism, Taoism, Islam (among ethnic minorities) and, most strikingly, given its foreign origins and relatively short history in China, Christianity. In the face of this onslaught, the party is beginning to rethink its approach to religion. It now acknowledges that it may even have its uses.

In Hongliutan the party appears in retreat. It is not the party secretary Zhang Tieniu who holds sway. Mr Zhang was the youngest party chief in the prefecture when he was appointed last year at the age of 32. But in a culture that reveres age, some villagers refer to him dismissively as a “lad”. The man in charge in Hongliutan is 64-year-old Wang Kehua. Mr Wang happens to belong to the village's main clan. He is also the village's elected chief (a post which in most villages is subordinate to that of party secretary). More to the point, he controls the temple and its money.

It was Mr Wang's idea to rebuild the temple in 1986, a decade after Mao's death. Mr Wang, who had become one of the village's wealthiest men by wheeling and dealing elsewhere, donated some of his own money and organised

villagers to add theirs. It was a promising venture. Historically, the Black Dragon Temple had a reputation extending far beyond the village. The dragon was renowned in the parched semi-desert of the north of Shaanxi Province, 600 kilometres (370 miles) west of Beijing, as a bringer of rain. If the temple was rebuilt, people would come, pray to the dragon—and spend money.

Mr Wang does not, however, speak of commercial motives. In the bare concrete-walled room he calls his office, he describes how, one after the other, the half-dozen villagers who had destroyed the temple in the 1960s fell victim to the vengeful dragon in subsequent years. The man who had broken off the head of the Black Dragon's effigy (the god is worshipped in a human-looking form, as shown in the picture above) had his head blown off when a factory boiler exploded. Another bled to death after accidentally chopping his foot with an axe. One was crushed by a donkey cart. Their offspring also suffered ill fate. These events, says Mr Wang, convinced him of the power of the dragon and of the importance of reviving its worship.

The temple has no clergy. Visitors are mainly drawn by their belief in the dragon's power to tell the future. Many want to know whether business ventures or marriages will succeed. Mr Wang asked the Black Dragon whether the divinity approved his appointment as temple chief. It did. The dragon's responses are given in the form of obscurely worded classical poems written on pieces of paper issued by a 70-year-old villager, Chen Yushan, clad in his blue padded Mao suit. Mr Chen offers his interpretation of what these poems mean. An entrepreneur who is told his business will be successful, and who then enjoys financial success, is quite likely to make a big donation to the temple.

Turning a blind eye

Officially, the party regards folk religion as superstition, the public practice of which is illegal. But in many rural areas officials now bend the rules. In Yulin prefecture, with 3.4m people, there are 106 officially registered places of worship and many more that are not officially sanctioned. Most are not part of the five mainstream religions (China regards the two Christian traditions, Catholicism and Protestantism, as separate) that the party recognises. But Yulin has allowed the Black Dragon Temple to affiliate itself with the government-sponsored Taoist Association. This gives it a cloak of legitimacy. So too does an arboretum that Mr Wang has planted with temple funds (at the dragon's request, he says, but it also helps him show officials how the village is contributing to government efforts to stop the desert encroaching).

Local officials themselves benefit from the greater tolerance. For all the party's dictatorial ways, government officers are often fearful of triggering unrest by enforcing unpopular policies that are not all that vital to the party's interests (hence the increasingly patchy implementation of population control). Demonstrations in an official's jurisdiction can do far more damage to his career than turning a blind eye to popular religion—so long as such activity does not directly challenge the party.

There are also more tangible rewards. In his book “Miraculous Response”, Adam Yuet Chau of the School of Oriental and African Studies in London says that temples applying for official registration typically have to treat local officials to banquets. Officials, he adds, support temples that pay them respect and tribute. They also gain financially from taxes levied on merchants who do business at temple fairs. Policemen invited to maintain order at these occasions are paid with cash, good food and liquor.

In the view of local officials, Mr Chau argues, temples play the same kind of role as commercial enterprises. They generate prosperity for the local economy and income for the local government. This is especially true of the Black Dragon Temple, which says it attracts 200,000 people to its ten-day summer fair (the Black Dragon himself, villagers say, has also shown up in the form of an unusually shaped cloud).

Evidence of China's religious revival can be seen throughout the countryside in the form of lavish new temples, halls for ancestor worship, churches and mosques (except in the far western province of Xinjiang, where the government worries that Islam is intertwined with ethnic separatism and keeps tighter rein). Officially there are more than 100m religious believers in China (see table), or about 10% of the population. But experts say the real number is very much higher.

This does not mean that China has embraced religious freedom. Some religions—Tibetan Buddhism, Islam as practised in Xinjiang, Catholicism and “house church” Protestantism, which involves informal gatherings of believers outside registered churches—are still subject to tight controls because of the party's fears that their followers might have an anti-government bent. A seven-year-old crackdown on Falun Gong, a quasi-Buddhist sect that flourished in the 1990s, is still being pursued with ruthless intensity. Many Falun Gong practitioners, as well as lesser numbers of followers of other faiths who refuse to accept state attempts to regulate their religions, are imprisoned in labour camps.

Within the party, however, debate is growing about whether it should

take a different approach to religion. This does not mean being more liberal towards what it regards as anti-government activities. But it could mean toning down the party's atheist rhetoric and showing stronger support for faiths that have deep historical roots among the ethnic Han majority. The party is acutely aware that its own ideology holds little attraction for most ordinary people. Given that many are drawn to other beliefs, it might do better to try to win over public opinion by actively supporting these beliefs rather than grudgingly tolerating them or cracking down.

The permitted five

Religion in China*

Religion	Adherents m	Clergy '000	Places of worship
Buddhism	100	200	20,000
Islam	20	40	30,000
Taoism	na	25	1,500
Protestantism	16	18	55,000
Catholicism	5	4	4,600

Sources: *China Daily*; Chinese Foreign Ministry; 1997 government White Paper

*Latest available official estimates

Pan Yue, then a senior official dealing with economic reforms and now deputy director of the State Environmental Protection Administration, argued in an article published in 2001 that the party's traditional view of religion was wrong. Marx, he said, did not mean to imply that religion was a bad thing when he referred to it as the opium of the people. Religion, he said, could just as easily exist in socialist societies as it does in capitalist ones. He also singled out Buddhism and Taoism for having helped to bolster social stability through successive Chinese dynasties. Stability being of paramount concern to the party today, Mr Pan's message was clear.

In praise of harmony

His article angered party conservatives at the time: the party's official stance is that religion will die out under socialism. But more recently the party itself has begun to put a more positive spin on the role of religion. Last April China organised a meeting of Buddhist leaders from around the world in the coastal province of Zhejiang (it did not, however, invite the Dalai Lama, Tibet's exiled spiritual leader). The event was given considerable prominence in the official media. The theme, “A harmonious world begins in the mind”, echoed the party's recent propaganda drive concerning the need for a “harmonious society”. It implied just what Mr Pan had suggested— that the opium Marx was talking about should be seen as a benign spiritual salve. In October the party's Central Committee issued a document on how to build a harmonious society, arguing that religion could play a “positive role”.

The party's change of tone coincides with its recent efforts to revive traditional culture as a way of giving China, in its state of rapid economic and social flux, a bit more cohesion. The term “harmonious society”, which in recent months has become a party mantra, sounds in Chinese (*hexie shehui*) like an allusion to classical notions of social order in which people do not challenge their role in life and treat each other kindly. It is, in effect, a rejection of the Marxist notion of class struggle.

Officials are now encouraging a revival of the study of Confucianism, a philosophy condemned by Mao as “feudal” and which can be quasi-religious. Since 2004 China has sponsored dozens of “Confucius Institutes” around the world, including America and Europe, to promote the study of Chinese language and culture.

In the countryside the revival of traditional values has needed little encouragement. Clan shrines, where ancestors are worshipped, have sprung up in many rural areas, particularly in prosperous coastal and southern regions. The revival of clan identity (in many villages a substantial minority, if not a majority, of inhabitants have the same surname, which they trace back to a common ancestor) has had a profound impact on village politics. Those elected as village leader often owe much of their authority to a senior position in the clan hierarchy. Control of the ancestral shrine confers enormous power. It is often clan chiefs, rather than party officials, who mediate disputes. The shrine will lend money for business ventures—so long as the recipient has the right name.

Where Christianity is a feminist issue

Ironically, the growth of clan power has helped to fuel the growth of Christianity in some parts of the countryside. In a village in the eastern province of Shandong, the wife of a former party secretary was a Protestant who attended prayer meetings with her female friends. Their religious enthusiasm was apparently fuelled by the subordinate role of women in the clan. A married woman is expected to revere only her husband's ancestors but is excluded from his clan hierarchy. The fast growing house-church communities often disapprove of ancestor worship, thus attracting women who feel fettered by clan strictures.

The parlous state of China's health-care system has also given a powerful boost to religion. Falun Gong owed much of its success in the 1990s to claims that it could heal without the need for medicine (cash-strapped state-run hospitals usually sell medicines to patients at inflated prices in order to boost their revenues). In the village of Donglu in Hebei Province, about 140km south of Beijing, Catholic nuns have set up a three-storey clinic where they offer ophthalmic, dental and pediatric services for what they say is a fifth of the price of government-run clinics or private ones run for profit. A picture of Jesus is pasted to the wall in the operating theatre.

An apparition of Mary is said to have occurred in Donglu in 1900 when local Catholics were fighting off an assault by members of the fanatical Boxer cult trying to destroy their church. This has made the village a site of great devotion

for Catholics. Every May for the past decade, the police have cordoned off Donglu to prevent thousands of Catholic pilgrims making their way to the village to celebrate the feast of Mary. Many of the pilgrims are loyal to an underground church which claims closer ties with Rome than the state-approved Catholic church. Yet for all Donglu's sensitivity, the local government appears content to let Catholics run the hospital, which is a key public service.

Chinese officials are even urging religious organisations to learn from Hong Kong, where religious groups run many schools and hospitals. In late November, Ye Xiaowen, the head of the State Administration of Religious Affairs which oversees the five officially recognised religions, said that religious groups had helped reinforce social stability in the former British colony with their contribution to public services. The Archbishop of Canterbury, Rowan Williams, who visited China in October, wrote afterwards in the *Times* that there was now a sense in China that civil society needed religion, with its motivated volunteers. During his trip he remarked on an “astonishing and quite unpredictable explosion” in Christian numbers in China in recent years.

The party still mouths its alarmist rhetoric about what it says are foreign efforts to use religion as a means of undermining the party's grip on power. Yet the appointment of Pope Benedict XVI, following the death in 2005 of John Paul II who was seen by China as a more die-hard anti-communist, has encouraged tentative efforts by China to restore the ties with the Vatican that were severed in 1951.

Last month the Vatican decided to appoint a commission to handle Chinese relations. But progress has been far from smooth. On November 30th, much to the Vatican's annoyance, China's state-backed Catholic church appointed a bishop without the Vatican's prior approval for the third time that year. Since 2000 China had done so only with the Vatican's tacit assent. In August, however, China released a bishop loyal to the underground church, An Shuxin, who had been arrested a decade earlier after leading celebrations of the feast of Mary in Donglu.

An even more tentative rapprochement is under way with the Dalai Lama. Since 2002, China has held five rounds of talks with his representatives, most recently last February. But China retains profound fears that the Dalai Lama's real intention is to separate Tibet, and adjoining areas, from China (see article). Notwithstanding the government's suspicions, Tibetan Buddhism has acquired a certain chic in Chinese cities in recent years, with some urbanites regarding it as spiritually more pure than Chinese-style Buddhism, which has strong links to the government.

AFP

Worshipping behind a shield of incense

Within its own ranks, the party knows that some members practise religion even though this is against the party's rules. Falun Gong claimed many adherents among party members in the 1990s. In the countryside, party secretaries routinely take part in religious ceremonies. Mr Wang at the Black Dragon is not a party member, but in other villages in the region temple chiefs double up as village party bosses. If the party is still trying to keep its members atheist, it is fighting a losing battle.

One result of allowing religion to play a bigger role in providing education could be that the party finds its efforts to inculcate its ideology among the nation's youth becoming ever more frustrated. In Hongliutan, the temple-sponsored middle school attracts many boarders from the town—a reversal of the normal flow of village pupils to the towns. Thanks to the temple's sponsorship, the middle school's fees are half of what they would be at a government school, teachers say. With this sort of discount, the popularity and influence of the Black Dragon, and other such spiritual beasts, seems certain to spread.

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About sponsorship

Correction: Indian cotton

Feb 1st 2007
From The Economist print edition

An article on farmers' suicides in India ("The great unravelling", January 18th) described Vidarbha's cotton farmers as "mostly illiterate". But according to an inquiry by the Tata Institute of Social Sciences, only about a fifth of those committing suicide in Maharashtra state were illiterate. We apologise. This error has been corrected online.

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About sponsorship

Developing cities

The lowdown on Motown

Feb 1st 2007 | DETROIT, MICHIGAN
From The Economist print edition

AP

Can anything revive Detroit after its long, depressing slide?

CALL it a tale of two bars. When Sean Harrington opened the Town Pump Tavern in the mid-1990s, downtown Detroit was going through some of its worst times yet. The urban population had already fallen from 1.8m in 1950 to less than 1m in the 1990s, and the tax base with it, after decades of middle-class flight (both black and white) to the suburbs. The American economy was booming, but Detroit's prospects were grim. Poverty, high unemployment, crime, racial tensions and an air of abandonment all seemed unfixable in a city that was tied to domestic carmakers, shrinking rapidly and written off by suburbanites.

Even though the corner that Mr Harrington chose for the Town Pump was right in the theatre district, previous use of the space gave him little reason for cheer. Since Detroit's race riots in 1967, the place had been set on fire by its owners and had then been variously used as a coin-operated laundry, a meeting place for self-help groups and a home for citizen crime-fighters. Mr Harrington started a beer-and-burger joint and hoped for the best.

By contrast, the bar that he opened across the street 18 months ago is a far more upscale affair. The Centaur Bar serves 18 kinds of martinis—in a bold art-deco setting—to a well dressed, racially diverse and upbeat group of young professionals. Mr Harrington is now putting in studio flats above the bar, and his first tenant is an entrepreneur whose company makes shark-fin antennae, an increasingly popular car part: just the sort of person one would expect to live in trendy suburbs such as Royal Oak or Ferndale. It is hard for a present-day visitor to imagine what preceded the Centaur. The place had been a wine and beer shop, with bulletproof glass and bars across the windows.

Although these may be the best of times for Mr Harrington, his bar is a rare sign of hope in a city that remains desperate for them. Detroit's property developers, city officials and boosters eagerly point to a few others. Many are on or near Woodward Avenue, which runs north-west from the river through downtown. Along that promising stretch—which goes through the theatre district and near some renovated sports stadiums—new restaurants, office spaces and the odd bookstore or shop offer evidence of the few thousand people with spending money who have moved into flats downtown.

Three casinos have also been built in the city, and attract enough visitors to boost Detroit's annual tax revenues by more than $100m. “We have become very dependent on them very quickly,” says Kurt Metzger, a local research director for the United Way, a charity.

Much hangs on a 5 ½-mile (9km) length of riverfront that is being overhauled by a huge public-private venture. It will include a state park and lots of space to walk, cycle and play. Developers plan to add places in between to live and work. In the middle of this stretch stands the Renaissance Centre, a giant tower of office, hotel and retail space that was revived after GM, one of the three big carmakers, decided in 1996 to buy it and install its corporate headquarters there. Although the riverside will remain a far cry from Chicago's lakefront—where one can look out on

clear blue water rather than Windsor, Canada—locals hope that the project will induce more high-income workers to live downtown instead of in the suburbs.

Matthew Cullen, who runs GM's global property portfolio and community-development efforts, says it made sense for the city and its corporate contributors to take on the whole riverfront at once. After an “economic fire” had wiped out Detroit's property values, there was a one-off chance to buy lots of land and redesign the whole stretch from scratch. Even many of Detroit's critics and pessimists agree that the riverside project is a good idea.

Kwame Kilpatrick, the mayor, also gets high marks from many business people and civic leaders for his efforts. He did not handle the job well in his first term, but he was only 31 years old when he took office. Since his re-election in 2005, he seems to have matured in the job. He is not beholden to either side in battles between unions and businessmen, or between downtown interests and those of surrounding districts. Moreover, Mr Kilpatrick does not face term limits, and increasingly seems to be taking the long view when dealing with Detroit's problems.

In fairness to the boosters, these isolated improvements do indeed offer Detroit its best chance in a long time to revive itself. A decade ago, says Mr Cullen, signs of hope were so scarce that “when they opened an International House of Pancakes it was front page news for a week.”

Doing better than before, however, is hardly the same as doing well enough to surmount Detroit's problems, which are immense. The city's finances are in desperate shape. Mr Kilpatrick has made cuts, such as shrinking the city's workforce, and handing over both a zoo and street-cleaning to non-profit groups. Yet Detroit's debt ratings remain only a notch or two above junk status. And since Michigan as a whole is also suffering from the car industry's slide, there is little the state could do to help even if voters wanted it to.

The racial divide

Although the recent trickle of new residents is heartening, large shopping centres and retail outlets remain a distant wish downtown. The unemployment rate in the city is above 14%. A 2005 Census Bureau study estimated that 31.4% of Detroit's residents were living in poverty, second only to Cleveland. Mr Metzger points out that only Hartford, Connecticut has a higher income gap between the city and the suburbs.

Unlike most other American cities, Detroit sends nearly as many commuters to jobs in the suburbs every day as it brings in. Increasingly, schoolchildren are following workers out of the city, often to attend charter schools: Detroit recently announced plans to close 52 of its public schools. All the while, some city council members act as though they would not mind if the downtown hollowed out completely—so long as the last person to leave got union wages and benefits for turning out the lights.

Racial divisions also remain a big problem. Nearly 90% of the city's residents are black, and most whites in the area live in suburbs. Of America's 318 official metro areas only Gary, Indiana is more racially segregated than Detroit. No matter what the question, the answer often involves race. Ask about activities that are reviving downtown, for example, and locals helpfully point out that both blacks and whites can find more things that they respectively like to do. Even setting race aside, resentment of high-income newcomers by low-income city residents could frustrate plans to get more people to move in.

In short, Detroit is heading in the right direction, but it has only gone a little way along what is clearly a long and difficult path. To outsiders, that may not seem much worth celebrating. But to some locals, who know how bleak life was before, it is a good enough reason to enjoy a few martinis and go and see a show.

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Urban crime

In Murder City

Feb 1st 2007 | NEW ORLEANS
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The white bourgeoisie make disturbing new targets

THE Democrats' new hope, Barack Obama, was in New Orleans this week, urging America not to forget the place. It is easy to do so. While ordinary law-abiding folk, obedient to the mayor's exhortations, are moving slowly back to the streets that Hurricane Katrina devastated 17 months ago, the criminal classes need no invitation. After a short hiatus, murder is as common in the city as it ever was.

In the first three weeks of January, 14 killings were reported. If the pace keeps up, the city will record well over 200 murders in 2007, an astonishing number for a place its size. New York, with at least 20 times as many residents as New Orleans, had 596 murders last year.

But the crisis is not just about numbers. Some of these murders were unsettling for a different reason. Helen Hill, a white, Harvard-educated, independent film-maker, was shot inside her home by a stranger. (Her husband, a doctor, was shot three times as he held the couple's two-year-old son; both survived.) That murder came a week after the killing of Dinerral Shavers, a high-school music teacher and snare drummer for the popular Hot 8 Brass Band, who was shot while driving. Mr Shavers's stepson, who was in the car with him, was the intended target. Murders in New Orleans usually revolve around the drug trade, and the victims are usually poor blacks. This time, middle-class residents have been caught up in them. And Mrs Hill was the sixth person killed within a single 24-hour period.

Unfortunately for Warren Riley, the police chief, that bloody day immediately followed a news conference at which he had tried to put a positive spin on the 162 murders recorded in 2006. It was the lowest number of killings in three decades, he said. Perhaps it was; but in 2006 the city's population, washed out by Katrina, was less than half what it was in the late 1990s.

The public felt patronised, and on January 11th 5,000 people marched on City Hall. It was the largest such demonstration in memory. As a result the mayor, Ray Nagin, made a list of public-safety promises: late-night vehicle checkpoints, a return to a few foot patrols, TV cameras in high-crime areas. Federal law-enforcement agencies have agreed to lend a few of their officers to New Orleans's beleaguered police department, and federal prosecutors have said they will try as many local criminals as possible in the federal courts. This is useful, as the district attorney's office is in disarray. One study by a local watchdog group found that in 2003-04 about one in eight people charged with murder or attempted murder was convicted. So far, police have made only one arrest for the January killings.

Murder has for too long been a part of city life. New Orleans, after all, is often credited with the invention of the “RIP shirt”—shirts worn as a tribute to youths who have died in violence, usually featuring the dead youth's face with a slogan such as “Lived like a soldier, died like a soldier.” From 1994 to 1999 the number of murders fell by almost two-thirds, a drop widely attributed to a vastly improved and enlarged police department. But New Orleans remained among the most dangerous cities in the nation, and the murder rate soon began to creep back up.

To make a permanent dent in the figures, New Orleans will have to address its underlying problems: one of the worst school systems in the country; an economy that offers few opportunities, particularly for the ill-educated; a flourishing drug trade; and a nihilistic youth culture in which guns are seen as acceptable tools for resolving disputes. The city fathers are well aware that unless the picture improves, those middle-class residents who are vacillating between rebuilding and moving out will not have much difficulty making up their minds.

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Economic policy

Raring to go

Feb 1st 2007 | WASHINGTON, DC
From The Economist print edition

George Bush revs up his economic agenda

“I WOULD suggest moving back. I'm about to crank this sucker up.” With those words, George Bush turned the key of a large tractor at the Caterpillar factory in Peoria this week. It was one of several appearances designed to show off America's economic strength and set out the president's priorities. As these were Mr Bush's first economic speeches since the Democrats took control of Congress, Washington's commentariat was looking closely for any signs of compromise.

The timing was perfect. Figures out on January 31st left little doubt that the economy was revving up. According to preliminary estimates, output grew by 3.5% on an annual basis in the fourth quarter of 2006, much faster than expected and up sharply from the third quarter.

Not surprisingly, Mr Bush did plenty of crowing: “There is one undisputed leader in the world in terms of economy, and that's the USA.” But beyond the boilerplate paean to tax cuts, his speeches this week were notable for their broader perspective.

From health-care policy to education, Mr Bush set out how government should help people reap the benefits of a dynamic economy rather than protect them from change. In a clear nod to the new political reality, Mr Bush raised favourite Democratic topics, including rising income inequality and soaring executive pay; but he rejected the solutions from the left.

“Income inequality is real,” Mr Bush said. “The question is whether we respond to [it] with policies that help lift people up, or tear others down.” Education and skills, he said, were the key to dealing with it. On executive pay, Mr Bush pushed for greater transparency. Shareholders ought to know exactly what the boss's pay is. (“The print ought to be big and understandable.”) He chided corporate boards for lack of attention, but argued against any government interference.

Most important, Mr Bush gave a robust defence of free trade. He stressed the importance of concluding the Doha round of global trade talks and explicitly asked Congress to extend trade-promotion authority (TPA), the negotiating mandate that presidents must have to conclude trade deals, which expires on June 30th. He urged lawmakers to resist protectionism (“Walling off America from world trade would be a disaster for our economy”); but in a nod to the new chiefs on Capitol Hill, he also admitted that “Global competition can lead to hardships.” He promised to work with Congress to improve trade-adjustment assistance, America's main federal scheme for helping workers displaced by trade.

For free traders this was all good news. Although a Doha breakthrough remains elusive, Mr Bush is engaged. On the day Mr Bush asked Congress to extend TPA, his agriculture secretary, Mike Johanns, unveiled proposed adjustments to the subsidies America lavishes on its farmers. His plan will respect any spending limits that result from a successful Doha round; it will try to forestall legal challenges at the World Trade Organisation; and it will divert some money to things like research and conservation that do not greatly distort trade.

All this makes a Doha compromise more likely. Whether the Democratic Congress will extend trade-promotion authority is less clear. Charles Rangel, the top trade man in the House of Representatives, is keen to get a TPA deal done, but only if Democratic concerns, particularly about helping globalisation's losers, are taken into account. Mr Bush may have cranked up his economic agenda. Less obvious is whether Congress will jump aboard.

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The presidential race

Ever Hopeful

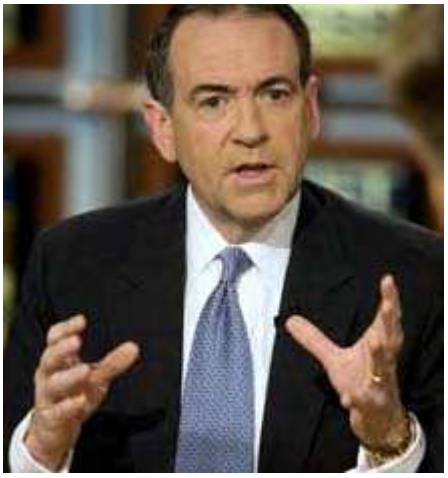
Feb 1st 2007 | LITTLE ROCK
From The Economist print edition

Mike Huckabee throws his hat in

AS THE presidential field grows daily more crowded, the latest Republican to jump in offers one intriguing advantage. He was born in Hope, Arkansas.

Mike Huckabee, ex-governor of Arkansas, has closely shadowed the last man of note to have been born there. When Bill Clinton became president in 1992, Mr Huckabee had just been thrashed in a run for the Senate. His political prospects were bleak. He ran again in 1993 in a special election for lieutenant-governor and won, against a Clinton ally, by just over 1% of the vote. He was re-elected in 1994 and then, when Governor Jim Guy Tucker resigned from office in 1996 after a felony conviction in the Whitewater scandal, Mr Huckabee became governor. In 1998 he was re-elected by a landslide, rare indeed for a Republican in this neck of the woods.

Reuters



Fighting off the Clinton shadow

This 51-year-old Southern Baptist minister is now about to fight an uphill battle. He has no money to speak of and is barely known, save for marathon running, dieting and living briefly in a mobile home while the governor's mansion was being repaired. Like any seasoned politician, he also has the odd small cloud hanging over him. But the problem that may haunt Mr Huckabee most has yet another Clinton connection.

In 1985 Wayne Dumond was convicted of raping a teenager, a distant cousin of Mr Clinton's. In 1992 Mr Tucker reduced Mr Dumond's life sentence, which allowed for parole. In 1996 Mr Huckabee planned to release Mr Dumond on lack of evidence, but relented. Mr Dumond left prison three years later and moved to Missouri, where he murdered a woman.

Critics say Mr Huckabee pressured the parole board to release Mr Dumond and grant clemency to others: therefore, he is soft on crime. Mr Huckabee retorts, proudly, that he has carried out more executions than any other governor in Arkansas history. And he denies that he leaned on the parole board.

Conservative groups are also annoyed by Mr Huckabee's support of five tax increases (though one of them was court-ordered, to improve the state's schools). He counters that he also supported 90 decreases—while still providing health insurance, under the ARKids First programme, for more than 70,000 children who otherwise had none.

Mr Huckabee talks of “horizontal” and “vertical” politics. Horizontal politics means the bad old ways: Democrat versus Republican, or liberals against conservatives. Vertical politics means that people forget their differences, and their leaders elevate them as a whole. Mr Huckabee's two most admirable vertical presidents are John F. Kennedy and Ronald Reagan. The other man from Hope inclined more to the horizontal.

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About sponsorship

Immigrants in the armed services

The green-card brigade

Feb 1st 2007
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How to become an American, via Iraq

ON January 11th Robert Gates, the secretary of defence, proposed increasing the size of the army and marines by 92,000 troops over the next five years. Doing so will be a challenge. Recruiters have thought of everything: higher enlistment bonuses, lower standards, turning a blind eye to the tattooed and the overweight. Now, how about focusing on foreigners?

Immigrants have fought in America's armed forces since the country first fielded one. Today, according to the most recent statistics, there are roughly 30,000 non-citizens on active duty and another 11,000 in the reserves. They come from more than 200 countries, with notable contingents from Mexico, the Dominican Republic, Jamaica and El Salvador. Several thousand are deployed in Iraq and Afghanistan. With very few exceptions, a foreign citizen must have a green card to enlist.

Recruiting non-citizens has clear benefits. Highly motivated soldiers should make dedicated and deserving Americans. And some non-citizens come equipped with useful languages. It takes over a year to teach a soldier Arabic, Pashto, or Dari from scratch. Native speakers can be deployed much more quickly.

These advantages have not gone unnoticed. In 2002 George Bush issued an executive order saying that non-citizen soldiers would in future be eligible to apply for expedited citizenship after serving one day on active duty. Previously, they had to wait several years. Since then, thousands of soldiers have been naturalised, and more than 80 have received posthumous citizenship. The armed forces have tried to bridge the language and culture gaps that can thwart recruitment. During last year's World Cup, for example, the army advertised on Arab Radio and Television.

The idea of recruiting immigrants to serve has its critics. Some argue that these soldiers would, in effect, be mercenaries. Others worry about immigrants taking risks that most Americans avoid. But maybe the current approach does not go far enough. Max Boot of the Council on Foreign Relations has proposed setting aside the requirement that foreigners hold a green card, and recruiting illegal immigrants as well as foreign citizens overseas. “We're looking to increase the size of our military, and this would be the most practical way to do it in the short run,” he says. And perhaps a way of tackling the immigration problem, at one fell swoop.

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Military discipline

Getting away with it

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Tougher sentences for some soldiers, but not for others

ON JANUARY 25th a soldier in the 101st Airborne Division was sentenced to 18 years in prison. He had pleaded guilty to murdering an Iraqi detainee and taking part in the killing of two others during a raid on the Muthana chemical complex last May. A fortnight earlier, another soldier involved in the same incident had been handed an 18-year sentence after pleading guilty. In November James Barker, also from the 101st Airborne Division, was sentenced to 90 years' imprisonment after pleading guilty to the rape and murder of a 14-year-old Iraqi girl, followed by the murder of her parents and a younger sibling, in the village of Mahmudiya, south of Baghdad, last March. Three other soldiers from the 101st division are awaiting trial on the same charges.

Are the military authorities becoming less tolerant of soldiers' bad behaviour abroad? Yes and no. Apart from Corporal Charles Graner, sentenced in January 2005 to ten years' imprisonment for his lead role in the Abu Ghraib scandal, almost no other American found guilty of the murder or abuse of Iraqi and Afghan civilians or detainees has received more than a couple of years in prison. Most have been demoted, had their pay docked, or simply been reprimanded.

Only last week, two Special Forces soldiers received reprimands after being cleared of wrongdoing in the deaths of two detainees at an American army base in Afghanistan in March 2003. Jamal Naseer, an 18-year-old Afghan army recruit, died after interrogation at the base; Wakil Mohammed, a woodcutter, died in American custody after being shot in the face during a search. Army investigators said the soldiers had shot him in self-defence.

Seven marines and a navy corpsman were charged with the unprovoked murder in April 2006 of an unarmed Iraqi civilian in Hamdania, a Sunni village west of Baghdad. Three have been given prison sentences of 12-21 months after pleading guilty to the lesser charge of aggravated assault; a fourth is awaiting sentence after pleading guilty to premeditated murder last month. The soldiers are alleged to have dragged the disabled 52-year-old man from his home, bound and gagged him, and shot him at point-blank range. They then made it look as if they had killed him in an exchange of gunfire as he was digging a hole for a roadside bomb.

Five months earlier, in one of the worst atrocities to come out of the Iraq war, 24 civilians, including women and children, were shot by American troops in the farming town of Haditha in apparent revenge for the killing of one of their squad by a roadside bomb. The marines claimed at first that most of the victims had been killed in the bomb blast and the rest as they tried to flee. Eight are awaiting trial after being charged in December.

So incensed was Nuri al-Maliki, Iraq's prime minister, by such atrocities that he called last July for a review of the law that gives immunity from prosecution to American troops. “Those who are free from being punished misbehave and they have misbehaved a lot,” he said. “The crimes in all these places [Abu Ghraib, Mahmudiya, Haditha and Hamdania] stink,” he added.

America has always insisted that it will carry out its own investigations and prosecutions into “credible” allegations of murder and serious maiming or abuse of innocent civilians. And in many cases, to its credit, it has done so. But until last July there was no requirement for officers to conduct such investigations.

According to American civil-liberties groups such as Human Rights First and Human Rights Watch, only about half the hundreds of allegations against American troops and personnel have been adequately investigated. The groups claim to have documented more than 330 credible cases of torture, killings and abuse of some 460 detainees in Iraq, Afghanistan and Guantánamo Bay. But of the 600 or so American soldiers and officials they say are implicated, only a tiny fraction—40 at the time of their report last April—had been given custodial sentences.

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Conservation in Colorado

Mountains for the centuries

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Clever ways to save land in the newly populous West

THE wide open spaces of the American frontier are much more crowded than they used to be. How, then, can open space be preserved? In Colorado, many different interests recognise that this is a pressing obligation. “For the Colorado economy it is an essential value,” says Mark Falcone, a Denver-based developer and board member for the Nature Conservancy's Colorado chapter. “Everything is linked to the landscape and the recreation it provides.”

Throughout the state, local and state-wide land-protection organisations (land trusts) are compensating for diminishing federal funds by working with the state legislature to provide economic incentives for land conservation. As Dan Pike, vice-president of the Colorado Coalition of Land Trusts, puts it, “We are giving landowners another choice about what they can do with their land.”

One innovative way to do this is to offer landowners a state income-tax credit in exchange for a conservation easement on their property. This easement, made between a landowner and a conservation organisation, maintains the private ownership of the property while permanently prohibiting certain types of development.

Tax deductions for conservation easements are not new. They have existed at federal level since 1976, and several states offer them. But Colorado is one of the most generous, remarkably so for a state not always known for caring for the environment. It offers an income-tax credit of 50% of the fair market value of the easement to a maximum of $375,000.

These credits are also impressively flexible. Income-tax credits may be fine for the Hollywood millionaires who own expansive tracts of land near mountain resort communities like Aspen and Vail; but they have limited appeal for the many Colorado ranchers and farmers who have little income for the state to tax. Such people, land-rich but cash-poor, may now submit their credits to the state treasury for a full cash refund whenever the state budget is in surplus. Or (budget surpluses being rare in recent years) they may sell them, at between 80 and 85 cents to the dollar, to a buyer who pays more in Colorado income taxes.

The legislation has had a massive impact. According to a recent national census report published by the Land Trust Alliance, the total acreage protected in Colorado increased from just under 350,000 acres (142,000 hectares) in 2000 to almost 1m by the end of 2005. As outright land purchases have decreased, conservation is increasingly becoming an easement business. Colorado Open Lands, one of 39 local and statewide land trusts, processed between eight and 12 conservation easements in 2002. Last year, they processed 43. As of December 2006, the Colorado Coalition of Land Trusts conservatively estimates that 1.2m acres of land are now protected under easements.

The law seems to have few enemies. Even conservatives like it. However, its cost in tax revenue is raising eyebrows. Annual revenue loss from the credits rose from a mere $2.3m in fiscal 2001 to $85.1m in 2005. Meanwhile, the state legislature and the general public have no idea how much land is being saved or even where it is. Some transactions are fraudulent, and there is not much regulation of valuations. Colorado, overstretched, is passing responsibility for these to the federal Internal Revenue Service, which has conducted 250 audits on Colorado easement transactions in the past 14-16 months.

Local land trusts sympathise with the criticisms, but see no need to end the programme. Revenue losses are offset by the fact that open space drastically increases the property value of nearby urban development. And, most important to conservationists, land is being protected in record amounts. Those in the business believe they cannot afford to wait; for no one knows how long Colorado's conservation gold rush will be allowed to go on.

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Lexington

Black power

Feb 1st 2007
From The Economist print edition

Kevin Kallaugher

America's blacks have growing political clout. They need to use it to confront some difficult questions

IT IS hard to remember a time when black America has been in such a prime political position. Barack Obama is the first black candidate to have a serious chance of winning the presidency (latest polls show him beating both John McCain and Rudy Giuliani in a head-to-head contest). And even if he fails this time round, he is likely to remain on the top rung of American politics for decades to come—perhaps as a vice-presidential candidate in 2008, and probably as a presidential candidate later.

Mr Obama is only the start of it. The Democratic takeover of Congress has dramatically increased the clout of the 43-strong black caucus. Members of that caucus chair five congressional committees and at least 14 subcommittees. Charles Rangel, a wily New Yorker, is in charge of the Ways and Means Committee, arguably the most powerful in the House; James Clyburn is majority whip, the third-ranking Democrat in the chamber.

Black America has something even more important than committee chairs: leverage. The two leading Democratic candidates, Hillary Clinton and Mr Obama, are both eager to court the black vote. Mr Obama needs to combat the suspicion that he is “not black enough”. Joe Biden may look like a buffoon when he says that Mr Obama “is the first mainstream African-American who is articulate and bright and clean”; but many civil-rights activists worry that he is not one of them.

Mrs Clinton is also making a determined bid for black votes. She is currently doing much better among black voters than Mr Obama is: a recent ABC News/*Washington Post* poll puts her support at 60%, compared with 20% for Mr Obama. She also has a large number of black leaders in her pocket. Blacks were a vital part of her husband's coalition—so much so that Toni Morrison dubbed Bill Clinton the first black president—and the Clinton machine will fight to keep it that way.

On top of this, there is more competition between Democrats and Republicans for the black vote than at any time since the Civil Rights Act of 1964. George Bush has made two black people in a row secretary of state—a far more elevated job than the Democrats had ever found for their most loyal supporters—and has increased aid to Africa. Ken Mehlman, the recently retired Republican Party chairman, put courting black voters near the top of his list of priorities. Last November the Republicans fielded black candidates for three major jobs, a Senate seat in Maryland and two governorships, in Ohio and Pennsylvania.

Opportunities like this do not come along every day. Black Americans will undoubtedly seize the chance to focus resources and attention on their problems. But they need to do more than this. One easy lesson is to start playing the two-party system to their advantage. It is understandable that blacks should have turned against the

Republicans after the debacle of Hurricane Katrina: even good black candidates, such as Maryland's Michael Steele, did badly in November. But it is nevertheless foolish to pledge your votes to just one party.

Blacks also need to start rethinking many of the policies that they have inherited from the civil-rights era. There are signs that 77-year-old John Conyers, chairman of the House Judiciary Committee, will use his power to sound old civil-rights tunes and to raise some crowd-pleasing issues, such as reparations for slavery. But black America needs to go beyond these ancient favourites and ask much harder questions.

The era of affirmative action, or preferential treatment for blacks, seems to be drawing to a close. It has always been unpopular with the majority of Americans: 58% of voters in Michigan wanted to restrict the policy in a ballot in November 2006. The Supreme Court has been able to defend the practice only by producing some implausible guff about “diversity”. And the new conservative majority is unlikely to let that nonsense endure for much longer. But what should replace it? Ideally, something quite different. Black Americans now have a chance to support policies, such as school vouchers and charter schools, that help not only themselves but other people; and that treat blacks not as an underprivileged caste, but as individuals.

This new attitude means holding blacks to the same standards as everybody else. Bill Cosby, a black comedian, was roundly denounced for “blaming the victim” when he said that there was something desperately wrong with black street culture. But he had a point. That street culture is not only a symptom of a deeply dysfunctional society; it also helps to perpetuate what it celebrates. Mr Cosby's solution to the problem—holding each individual accountable for his or her behaviour regardless of race—is not blaming the victim. It is common sense.

Beyond victimhood

A new attitude also means recognising that the old policies have had a perverse effect: the huge gains that blacks have experienced since the Civil Rights Act have been unevenly distributed. A black middle class and a comfortable black establishment have emerged: about 1.1m blacks earn more than $100,000 a year. But a black underclass is also evident: people who are trapped in poverty by failed schools, broken families and endemic crime. Almost half of all black children are being raised by two parents, and a third of them are being brought up in poverty, compared with one-seventh of white children.

The paradox is that black Americans will be better off if they act less like a racial pressure group. This means focusing economic aid on the plight of the underclass—black, white or brown—not on blacks in general. Blacks will be disproportionate beneficiaries of this approach because they make up a disproportionate part of the underclass. The best use of black America's new political power is to stop thinking so much in terms of race, which is a diminishing problem, and start thinking in terms of class, which, alas, is a rapidly growing one.

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Venezuela

Glimpsing the bottom of the barrel

Feb 1st 2007 | CARACAS
From The Economist print edition

Reuters

Lower oil prices threaten Hugo Chávez's expensive revolution. But he is not about to run out of cash soon

Get article background

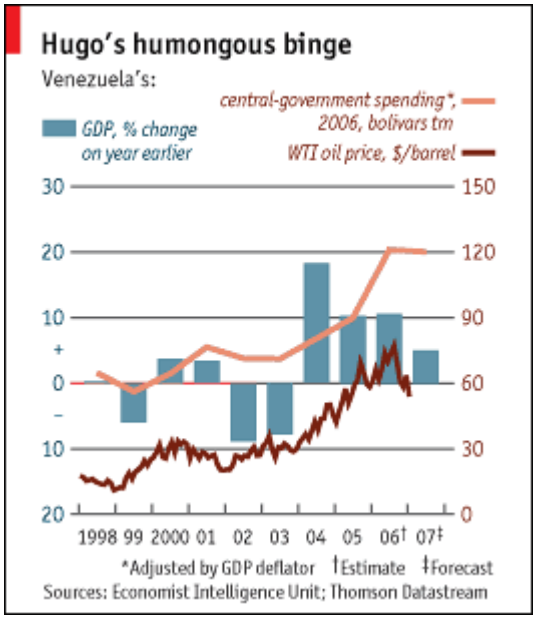
HE LOOKS unstoppable. Since his sweeping victory in an election in December, Venezuela's leftist president, Hugo Chávez, has stepped on the revolutionary accelerator. Parliament this week gave him the power to legislate by decree for 18 months. A committee of his supporters is drafting a constitutional reform to turn Venezuela into an avowedly socialist country, and to allow the president to stand for re-election indefinitely. “Nothing can stop the revolution!” proclaim full-page advertisements in the newspapers, adorned with the newly-minted red star of Mr Chávez's “Bolivarian socialism”. Nothing, that is, except perhaps a decline in the price of oil, on which the government depends for nearly half its revenue.

It has been Mr Chávez's extraordinary good fortune that the price of oil increased more than sixfold since he took office in 1999 to its peak last year. That has allowed him to ramp up public spending. With private investors scared off by controls and Mr Chávez's socialist talk, it is this spending binge that helped the economy recover after an opposition-led two-month general strike in 2002-03 and has since fuelled rapid economic growth (see chart).

So a lower oil price threatens economic growth, and with it Mr Chávez's popularity. Already, official projections and independent forecasts suggest the rate of growth may halve this year (but to a still-healthy 5%). Venezuelan crude, much of which is heavy and sulphurous, sells for about $10 less than lighter benchmark crudes such as Brent and West Texas Intermediate. Last year the average price for the Venezuelan “basket” of crudes was $56 a barrel. Last month, that figure was about $46. Any further fall might start to constrain Mr Chávez's ability to spend freely at home and abroad.

The 2007 budget is conservatively based on an average price for the Venezuelan basket of $29. But it is also based on average oil production of around 3.4m barrels a day (b/d). Neither of these figures bears much relation to reality and nor does the budget itself. Independent analysts, including OPEC and the International Energy Agency, believe the true production figure to be around 2.5m b/d. To complicate matters further, some of the oil is sold at a discount as part of Mr Chávez's strategy to win influence abroad, and 100,000 b/d is more or less donated to Cuba.

In contrast, total government spending last year was a third higher than originally budgeted. That pattern is likely to be repeated this year. “Quasi-fiscal” or off-budget spending, involving the diversion of oil revenues and the central bank's reserves into funds directly controlled by the president, is large and increasing.



Mr Chávez has a large piggy-bank he can draw on. The forthcoming constitutional reform is likely to strip the central bank of its last vestiges of autonomy. Between them, the bank's reserves and the resources of the National Development Fund total around $50 billion—a similar amount to this year's official budget.

So even if oil prices remain below their 2006 levels, nobody expects the bottom to fall out of the economy this year. But Mr Chávez needs not just to maintain public spending but to increase it if he is to satisfy the popular expectations he has whipped up at home, and to fulfil the pledges of aid he has made to friends abroad. In the past few weeks alone, he has promised to build 200,000 houses in Nicaragua and loan $1 billion to Ecuador, for example.

The economy is showing some signs of strain. The inflation rate, at 17% last year, was the highest in Latin America—even though Venezuela's currency is overvalued. Despite the oil bonanza, the government has run a fiscal deficit in most of Mr Chávez's time in power: this year that deficit may reach 3% of GDP.

The president seems to be aware of the problems. He has urged OPEC to cut oil output further, to set a floor for benchmark prices of $50. On January 21st he announced his intention to increase petrol prices for the first time since he came to power. Petrol costs less than 5 cents a litre in Venezuela at the official exchange rate, but raising the price is politically sensitive. The government also plans tax increases. Officials insist that plans to nationalise the telecommunications and electricity industries, announced last month, will not trigger a fall in tax revenues, though opponents doubt that.

The oil price has crept back up over the past fortnight after a sharp fall. It may well rise further. Even if it does not, few expect the benchmark price to fall to its levels of 2003, let alone 1999. But if prices stay at their levels of the past month, some economists believe that Venezuela's economy will struggle. “There's a sustainability problem,” says Luis Zambrano, an economist at the Catholic University in Caracas. “More and more spending is needed to produce a [percentage] point of economic growth.” What will lubricate the revolution when the oil bonanza ends?

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Oil in Colombia

Bucking a trend

Feb 1st 2007 | BOGOTÁ
From The Economist print edition

A rare welcome for foreign oil companies

OTHER Andean countries, such as Venezuela, Ecuador and Bolivia, have all put the squeeze on foreign oil companies, with measures ranging from tough new contracts to outright expropriation. But Colombia is putting out the welcome mat.

Colombia shares much of Venezuela's geology. But its oil output is smaller; the last big oil find was by BP at Cusiana in the 1980s. Having been a modest oil exporter for two decades, it faces becoming a net importer unless new discoveries are made. That prospect has prompted President Álvaro Uribe's government to intensify its predecessor's wooing of foreign oil companies. Colombia now offers “among the best fiscal terms in the world”, says William Drennan of Exxon Mobil. These include a sliding scale of royalties varying with production and longer contract terms.

A flurry of investment in exploration to the tune of $1.5 billion a year is starting to produce results. In 2006, for the first time in years, net oil reserves increased slightly, to 1.51 billion barrels. A decade ago, industry analysts expected Colombia to become a net oil importer by 2007. Now that date has been pushed back to 2011, according to a study by Arthur D. Little, a consultancy. If current levels of investment are maintained, Colombia should maintain its oil self-sufficiency at least until 2015, says Armando Zamora, the director of the National Hydrocarbons Agency.

More than a dozen foreign companies are now looking for oil in Colombia. At the same time, Ecopetrol, the state-owned oil company, is operating in a more commercial fashion. It plans to offer 20% of its shares (worth perhaps $3 billion) to private investors. It has joined forces with Petrobras, a like-minded state oil firm, to explore a small field in Brazil.

Having got itself back on the oil map, Colombia hopes to be able to strike a harder bargain. Later this year it will auction contracts to explore offshore in the Caribbean. They will go to the companies that offer the government the biggest production share. Now all that is needed is another Cusiana.

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Mexico

Tortilla blues

Feb 1st 2007 | MEXICO CITY
From The Economist print edition

A hard lesson in pocketbook politics

THEY are eaten folded in tacos, fried in flautas, or rolled in enchiladas. And when there is nothing to wrap them around, they are eaten plain. They are Mexicans' daily bread. So when a shortage of white maize caused the price of a kilo of tortillas to double to eight pesos ($0.75 cents) or more in late December, that became the first big political headache for Felipe Calderón, Mexico's new president.

Nearly all Mexican tortillas are made of home-grown white maize, rather than the yellow variety that is more common in the United States. The growing popularity of subsidised ethanol across the border has prompted the price of yellow corn, quoted in Chicago, to rise by over 50% since October. So industrial users of imported yellow corn in Mexico (for animal feed and syrup) started buying white maize instead.

The government was slow to react. The tariff on imported maize is not due to disappear under the North American Free Trade Agreement until next year. But the government could have blunted the price rise by waiving the tariff or moving quickly to expand the tariff-free quota, says Luis de la Calle, a former trade official.

Mr Calderón did raise import quotas on January 18th, and agreed a voluntary price-cap with the biggest tortilla makers. But the political damage had already been done, and the price cap does not cover the small-scale tortilla makers patronised by many poorer Mexicans.

The opposition has seized on the issue. Supporters of Andrés Manuel López Obrador, narrowly defeated by Mr Calderón in last year's presidential election, joined a protest march on January 31st. Mario Alberto di Costanzo, an adviser to Mr López Obrador, wants the government to subsidise tortillas; he blames monopolistic importers for the price rise.

A previous government withdrew the subsidy on tortillas because it was indiscriminate. Officials point out that the higher price is good news for the rural poor, who grow maize.

Mexico's Federal Competition Commission is investigating the import and distribution of maize. But Eduardo Pérez Motta, the commission's president, says he thinks that import quotas rather than monopolies are to blame for the price spike. In other words, contrary to Mr López Obrador's claims, Mexicans would benefit from free trade in maize.

With other food prices rising too, the annual rate of inflation has edged up to over 4%, constraining the scope for interest-rate cuts. If tortilla prices stay high, the government may have to find other ways to help the poorest consumers. Few things are more politically damaging in Mexico than pain at the taco stand.

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Uruguay

The next Chile

Feb 1st 2007 | PUNTA DEL ESTE
From The Economist print edition

If only it allowed itself to be

WHEN Luis Alberto Lacalle was the president of the small South American republic of Uruguay in the early 1990s he came back from a trip to Chile and proclaimed: “I've just returned from the future.” Like Chile, Uruguay is one of Latin America's most solid democracies, with relatively effective public institutions. But where Chile has forged ahead with privatisation, free markets and open trade, Uruguay has stuck cautiously to its more egalitarian but slow-moving social democracy.

Uruguay was knocked off course by Argentina's economic collapse, which led to a run on its banks and a deep recession in 2002-03. It has since bounced back strongly. Now it has taken a small step down the Chilean road. On January 25th the left-wing government of President Tabaré Vázquez signed a trade and investment “framework agreement” with the United States—a potential first step towards a free-trade deal.

Many of the elements for rapid economic growth are in place. Unlike Argentina, Uruguay did not default on its debt. The traditional pillars of its economy—farming, tourism and finance—are all doing well. Foreigners are buying ranches. The tourist industry, centred on the seaside resort of Punta del Este, has added rising numbers of Europeans and Americans to its traditional Argentine clientele.

Some Uruguayans also hope that their country can attract new service industries, such as call centres and back-office work. They point to its educated workforce, strong legal protections for investors and tax breaks for such ventures. India's Tata Consultancy Services chose Montevideo, Uruguay's capital, as its worldwide base for Spanish-language business-service and software operations.

Two things hold Uruguay back. The first is that it is part of Mercosur, the trade group based on Brazil and Argentina which now includes Hugo Chávez's socialist Venezuela. Mercosur's relatively high tariffs add to the cost of imported machinery. To sign a free-trade agreement with the United States, Uruguay would need the consent of its Mercosur partners.

Businessmen complain that they are not getting many compensating benefits from Mercosur. Argentina has behaved in an un-neighbourly fashion over a huge new paper plant being built by Finland's Metsa-Botnia on the Uruguayan side of their riverine border. Argentina's government has done little to restrain protesters who have blocked the main bridge between the two countries during the peak tourist season this year and last. They claim the plant will pollute the river; a recent study for the World Bank found minimal environmental impact.

The second brake is political. The finance minister, Danilo Astori, is a moderate in the mould of Chile's ruling centre-left coalition. But the ruling Broad Front also includes powerful trade unions and old-line socialists. In return for their support for responsible macroeconomic policies, Mr Vázquez has held back from starting free-trade talks with the United States. He has also backed tougher collective-bargaining rules, and promised not to intervene if workers occupy workplaces. Most Uruguayans seem happy to leave large swathes of the economy—including telecoms, much of electricity, oil imports and several banks—in state hands.

Uruguayans “want to have a dynamic capitalism like Chile, but with more emphasis on equality,” says Adolfo Garcé, a political scientist at the University of the Republic in Montevideo. But Uruguay may have to choose between dynamism and egalitarianism.

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Canada's citizenship laws

Lost in Kafkaland

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When is a Canadian not a Canadian?

IN THE deathless prose of bureaucracy, it is known as the Western Hemisphere Travel Initiative. Adopted after the terrorist attacks of 2001, it requires all returning Americans, as well as citizens of Canada, Mexico and some Caribbean countries, to present a passport when entering the United States by air. Since many such travellers previously got by with a driving licence, it was dreaded by tourism officials in the countries concerned. But when it came into effect earlier this month, all seemed to go smoothly.

Except it didn't for several thousand Canadians who, when they applied for passports, discovered that their own country's bureaucracy had incomprehensibly stripped them of their nationality. Some of them have even become stateless.

Up to 20,000 people may have fallen foul of a little-known provision of the Citizenship Act of 1947. In some cases, their misfortune lies in having been born during the period when Canada did not recognise dual citizenship until the act was amended in 1977. Some are the children of war brides who came to Canada after the second world war. Others are “border babies” born in an American hospital because it was closer to their home than the nearest Canadian town. A third group are children of parents who moved to the United States for work and took out American citizenship. The law states that if any of these Canadians were living outside Canada on their 28th birthday (or 24th in the 1947 act) they would automatically lose their citizenship unless they filled out a form saying they wished to keep it.

One of many who knew nothing of this requirement is Barbara Porteous, a British Columbian born just over the border in Washington state. When she applied for a passport last July she was told she would first have to re-apply for citizenship. This would take three years, involve health and criminal checks and a C$125 ($106) fee. “It just blew me away,” she said. “I've been living here for 46 years and getting the Canadian pension for the past five years.”

Andrew Telegdi, a Liberal MP, dubs those affected “lost Canadians” and says they were deprived of their citizenship without proper notice. He is campaigning to reform the law. But like its Liberal predecessor, the current Conservative administration shows no inclination to do so. Diane Finley, the immigration minister, announced on January 24th that she had directed her department to resolve these cases as quickly as possible. That means about a year, her officials admit. It makes the complex immigration procedures at American airports feel like greased lightning.

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Indonesia

Old soldiers who refuse to fade away

Feb 1st 2007 | JAKARTA
From The Economist print edition

Indonesia's president is worried by the rumblings from former strongmen. But perhaps more worrying is the slowness of democracy to deliver results

Claudio Munoz

Get article background

TWO retired chiefs of Indonesia's armed forces have badly rattled Susilo Bambang Yudhoyono, the former general who became Indonesia's first directly elected president in 2004. Try Sutrisno and Tyasno Sudarto are publicly accusing the president of failing to solve the country's high unemployment and inflation. They, and other old soldiers, claim that the “chaos” in Indonesia justifies undoing the constitutional amendments that introduced direct elections for president and replaced a partly appointed parliament, packed with soldiers, with a fully elected one. Last month, on hearing that a rally was to be staged outside the State Palace to demand his downfall, Mr Yudhoyono cut short a foreign trip.

In the end the rally drew only a few hundred people. A poll taken a few weeks earlier showed that, despite high public dissatisfaction over the economy, the president's personal approval rating was 67%, which is higher than the share of the vote that won him the presidency three years ago. Nevertheless, Mr Yudhoyono has felt compelled to fight back. On January 25th he accused his detractors of trying to put the nation under a state of emergency and described their demands for a return to the old order as “ahistoric and illogical”.

Military bosses, who dominated politics under President Suharto's regime, have seen their power and perks chipped away since its downfall in 1998. Provincial and local governments used to be run by appointees, usually uniformed ones, but now both governors and mayors are elected. A large share of tax revenues has been transferred to local authorities, though so far with disappointing results: much has either been misspent or gone unspent. This has allowed those who lost out to complain that Indonesia's “experiment” in local democracy has failed.

The government is gingerly trying to prise from the army's hands the thousands of businesses it owns. These help to pay its regular expenses—but much of the money slips into officers' pockets. It has also been removing from the army those jobs that should belong to the police, such as anti-terrorism investigation. The harrumphing ex-strongmen, all army types, were irked when the president chose an air-force man, Djoko Suyanto, as his chief of the armed forces. They also dislike the proposals that would allow soldiers accused of ordinary crimes to be tried in civilian courts.

The military men have plenty of gripes but there seems little chance that they will take the law into their own hands. Alvin Lie, a parliamentarian from the small National Mandate Party, says that in the past the army “has only moved when the masses are moving” and there is no sign of such public unrest. A man who might have the charisma to whip up the masses, says Mr Lie, is ex-General Wiranto, another ex-chief of the armed forces, who has just formed a new party as his base for a shot at the presidency in 2009 (he was beaten by Mr Yudhoyono in 2004). But Mr Wiranto's party is stuffed with former military men and lacks democratic credentials.

Paul Rowland of the Jakarta office of the National Democratic Institute, an American think-tank, says that Indonesians are disappointed with Mr Yudhoyono's over-cautious style but believe him to be an honest man who is trying his best. They give him credit for not hiding himself away whenever there is a crisis, unlike his predecessor, Megawati Sukarnoputri (who, as it happens, is also plotting a comeback).

So far, the most plausible potential challenger to Mr Yudhoyono in 2009 is his vice-president, Jusuf Kalla, who is as decisive and impetuous as his chief is indecisive and circumspect. In some senses they are a good match but, says Muhammad Hikam, another parliamentarian, Mr Yudhoyono urgently needs to show he is boss. Mr Hikam argues that those who blame Indonesia's slow progress on the constitutional changes are wrong: rather, he says, it is all down to the “management failure” of the Yudhoyono administration.

Mr Lie is not so sure, believing that the process is also hampered by the extensive consultation that the current constitution demands. For the anti-discrimination bill that he is promoting, Mr Lie has had to spend a year staging forums around the country, inviting all interested parties to comment and carefully recording their responses. Otherwise the bill, even if passed by parliament, could be challenged in the constitutional court by anyone claiming to be injured. “It's one of the consequences of being transparent,” he sighs.

Indonesia has an enormous bureaucracy, which gobbles up one-eighth of all public spending. But much of it is dead wood. Mr Yudhoyono has tried to set up his own high-powered team, modelled on the West Wing of the White House, but this has met with resistance from ministries which see their turf threatened.

Indonesian democracy is still a work in progress. An authoritarian, centralised regime has been replaced with one whose elaborate checks and balances are only beginning to be tested. Some constitutional tweaks may be needed but, mainly, politicians and officials need more time to learn on the job. If Indonesians ever lose patience, they should look north to Myanmar and Thailand, to remind themselves that military men don't have the answers.

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Tibet

Still Tibetan after all these years

Feb 1st 2007 | LHASA
From The Economist print edition

Economic advance is not winning all that many hearts and minds

IT WAS an odd remark to come from a Chinese government official. Instead of flaunting the 13.2% growth that his autonomous region reportedly achieved in 2006, he was openly contemptuous of the calculations: “The officials tell us what incomes Beijing wants us to report and then we just have to report those numbers, even though there are farmers earning far less.” Worse, he has views on the limits of Chinese sovereignty. “Highest this in China, highest that in China,” he says, in a caustic imitation of Chinese tour guides. “This,” he declares, a hand sweeping out towards the mountain-circled horizon, “is not China. This is Tibet.”

He may work for the Chinese government, but he is an ethnic Tibetan and, like many others, he is intransigently opposed to all things Chinese. His motives in working for the party are purely mercenary: “It's the highest paying job I can get.” He also admits that he would like to visit India to see the Dalai Lama, Tibet's exiled spiritual leader. But, for now, he must earn money.

His is a common tale in modern Tibet: even as they take advantage of some of the economic opportunities Chinese rule has brought, many Tibetans remain staunchly proud of their own culture. This belies Chinese propaganda portraying supporters of the Dalai Lama and Tibetan separatism as a dwindling minority.

On the other hand, the official's story does not quite fit the image of modern Tibet fostered by China's critics. In their version, economic growth benefits only ethnic Han Chinese. China embarked in 2000 on a drive to accelerate development in its backward western regions, including Tibet. Since then, and especially since last year when a railway to Lhasa was completed, pessimists have been mourning in advance the death of Tibetans' unique Buddhist culture and identity.

Economic growth, it was argued, would bring a flood of Han Chinese immigrants, who would “Hanify” Tibet and murder its culture. But just as that culture survived China's invasion in 1950, the flight of the Dalai Lama in 1959 and the devastation of the Cultural Revolution in the 1960s and 1970s, so it is now resisting the subtler ravages wrought by economic progress.

China's western development policy in part reflects the government's belief that economic growth would quench demands for greater political liberty. If Tibetans grew richer, surely they would become friendlier to life under Chinese rule? And, indeed, some Tibetans are sharing the new wealth. Lhasa has become a magnet for Tibetans from across the plateau, drawn by the opportunities created there by the booming tourist industry for guides, vendors and hotel workers. Scholarships take Tibetan students to universities in Beijing and Shanghai.

Even outside Lhasa, some Tibetans acknowledge that Chinese economic policies have brought benefits. In the northern town of Nagqu, for example, nomadic herders now have houses to shelter them from the icy winter, thanks to economic progress and government aid. Recognising Tibetan poverty, the government recently announced that it would offer aid to more than 230,000 farmers and herdsmen. The statistics are fudged and many Tibetans are still

desperately poor, but on the whole they are better off than they once were.

Tibetan tradition has not survived unscathed. Some young people are abandoning nomadic life for lucrative urban jobs. Unworldly lamas now boast Nike caps. As one bitter gentleman puts it, “there are those who have sold out to the Chinese.”

But if the true index of a culture's vitality is its adherence to its language, historical memory and religious traditions, Tibetan culture shows itself durable. Loyalty to the Dalai Lama, the Tibetan language and a view of history in which the Chinese are illegitimate invaders will not die soon. Each year, thousands sneak across the border and receive “religious and cultural training” from the Dalai Lama's government-in-exile. Those who return pass the lessons to their compatriots.

Many of those who do not risk the journey to India work hard at preserving their Tibetan heritage. One mother says that she insists that her daughter learn Tibetan, and that many others do the same. “Chinese is important for work but Tibetan is who we are. If you come back to Lhasa in ten years, you'll see many more people speaking Chinese. But they would still be Tibetan.”

Such ideas pose no immediate security threat to China. But their persistence in the face of genuine danger highlights the limitations of Chinese rule. China has, through force, won reluctant submission. Acceptance, however, cannot be bought.

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North Korea and the internet

Weird but wired

Feb 1st 2007 | PYONGYANG
From The Economist print edition

Online dating in Pyongyang? Surely not

KIM JONG IL, North Korea's dictator, has interests in modern technology beyond his dabbling in nuclear weaponry. In 2000 he famously asked Madeleine Albright, then America's secretary of state, for her e-mail address. Mr Kim believes there are three kinds of fool in the 21st century: smokers, the tone-deaf and the computer-illiterate.

One of his young compatriots is certainly no fool. “Officially, our computers are mainly for educational and scientific purposes,” he says, before claiming: “Chatting on our web, I also met my girlfriend.”

Internet dating is only one of the surprises about the internet in North Korea, a country almost as cut off from the virtual world as it is from the real one. At one of the rare free markets open to foreigners, brand-new computers from China are sold to the local *nouveaux riches* complete with Windows software. Elsewhere, second-hand ones are available far more cheaply. In most schools, computer courses are now compulsory.

In the heart of the capital, Pyongyang, visitors are supposed to be able to surf freely through the 30m official texts stored at the Grand People's Study House, the local version of the Library of Congress. The country's first cyber café opened in 2002 and was soon followed by others, even in the countryside. Some are packed with children playing computer games.

But the world wide web is still largely absent. Web pages of the official news agency, KCNA, said to be produced by the agency's bureau in Japan, divulge little more than the daily “on the spot guidance” bestowed by Kim Jong Il. No one in Pyongyang has forgotten that *glasnost* and *perestroika*—openness and transparency—killed the Soviet Union.

The local ideology being *juche*, or self-reliance, the country installed a fibre-optic cable network for domestic use, and launched a nationwide intranet in 2000. Known as *Kwangmyong* (“bright”), it has a browser, an e-mail programme, news groups and a search engine. Only a few thousand people are allowed direct access to the internet. The rest are “protected” (ie, sealed off) by a local version of China's “great firewall”, controlled by the Korean Computer Centre. As a CIA report puts it, this system limits “the risks of foreign defection or ideological infection”. On the other hand, North Koreans with access to the outer world are supposed to plunder the web to feed *Kwangmyong*—a clever way to disseminate technical information to research institutes, factories and schools without losing control.

Yet even today, more and more business cards in Pyongyang carry e-mail addresses, albeit usually collective ones. A west European businessman says he is astonished by the speed with which his North Korean counterparts respond to his e-mails, leading him to wonder if teams of people are using the same name. This is, however, North Korea, and sometimes weeks go by in virtual silence.

In some places, North Korea's internet economy seems to be overheating. Near the northern border, Chinese cell phones—and the prepaid phone cards needed to use them—are a hot black-market item, despite government efforts to ban them. The new web-enabled phones might soon give free access to the Chinese web which, for all its no-go areas, is a paradise of liberty compared with *Kwangmyong*. In this region, known for its casinos, online gambling sites are said to be increasingly active.

Last summer the police were reported to have cracked down on several illegal internet cafés which offered something more daring than the average chatting and dating. Despite the signs that North Korea's web culture is ready to take off, internet-*juche* remains a reassuring form of control in the hermit regime.

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India's rickshaws

Colonial yokes are not bad for all

Feb 1st 2007 | KOLKATA
From The Economist print edition

The world's last rickshaw-pullers are battling against extinction

SOME very poor men, perhaps 18,000 of them, went on strike in Kolkata on January 24th to protest against a ban on their livelihood, ostensibly imposed for their own good. Much good may it do them. The Communist government of West Bengal has long wanted to outlaw rickshaws, of the original man-pulled variety, that now exist only in Kolkata. Last December it did so, on the grounds that man-powered transport was inhuman. But what else are the thousands of rickshaw-wallahs, in one of the world's poorest cities, to do?

Beg, is the best guess of a group of rickshaw-pullers on Debendra Ghosh Road, a typically crowded alley in central Kolkata. Like most of their fellows across the city, they are migrants from Bihar, India's poorest and third-most populous state. Earning around 150 rupees ($3.50) a day, with an average fare of 20 cents, they are not flush. But with an annual income of a little over $1,000, after paying rent on their rickshaws, they make roughly double West Bengal's average. “I may not like it, you may not like it, but I have children to feed,” said Mahendra Paswan, a rickshaw-wallah for 26 years, with bare feet, a blue-check lungi, and six offspring in school.

West Bengal's government sees the rickshaw trade as an outworn symbol of the colonial yoke. “A disgraceful practice that flourished when the British lorded over the people,” is how Buddhadeb Bhattacharjee, the chief minister, has described it.

The rickshaws are used by Kolkatans of all classes, especially in streets too narrow for taxis. But the chief minister, despite his Marxist mantra, has been furiously opening the state to business over the past six years. His vision, which includes making West Bengal one of India's top three producers of information technology by 2010, is apparently incompatible with the herd of “human horses” on Kolkata's streets.

The rickshaw-pullers are going down battling. When the government started destroying unlicensed rickshaws a few years ago, they formed themselves into a union to fight the ban. “We are all faced with ruin,” lamented Mr Paswan, who fears that cycle-rickshaws, which the government says it wants instead, are even more arduous to operate. In the meantime, Mr Paswan can offer a pleasant trot across Kolkata, an excellent way to view the city's fine colonial buildings.

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Hong Kong's preservation

Stardust memories

Feb 1st 2007 | HONG KONG
From The Economist print edition

An architecturally ruthless city is now wanting some of its past back

OTHER than a nice view of landfill on the fringes of Hong Kong's harbour, Queen's Pier is a bedraggled slab of cracking concrete and dirty white tiles, dimly lit at night by fluorescent tubes. For a city that has felt few qualms about destroying innumerable lovely colonial structures, it is an odd one to preserve. Odder still, the road planned in its place will be of far greater use, thereby meeting the standard the city has practised, to much public approval.

Yet, to the surprise of the government, the pier has found itself with throngs of defenders. They have been roused by the destruction in December of the adjacent Star Ferry terminal, another fairly nondescript building but one that, clearly, turned out to have been rather loved.

In quite un-Hong Kong fashion, protesters tried to close the building site at the pier with a chain. This was ineffectual, particularly since they kindly opened up for cars. Scaffolding surrounding the old ferry building remains strung with laundry lines holding up taped pictures. Signs read “It is wrong”, “Respect our history”, and “No history, no tomorrow”.

The slogans are striking. Hong Kong has always created its future by building over its past. The vast, technologically sophisticated, modern office towers packed with the bankers, lawyers and accountants who have made Hong Kong the financial centre of Asia are all built on the rubble of earlier generations of buildings. Hong Kong's government makes money from selling redevelopment rights, and this has played a huge part in keeping its taxes low and its appeal to business high.

Still, renewal has come at a cost. Hong Kong has a bold skyline. But close up, with a few exceptions the buildings are not distinctive, and are often plumped on top of identical shopping malls. Protests over the Star Ferry terminal followed less intense rumbling about the redevelopment of “wedding-card street”, a short alley known for its small printing shops visited by couples after their engagements. Several covered markets built in the 1930s are to be knocked down soon and some of the increasingly rare open street-markets, once part of the fibre of Hong Kong's life, will also be lost.

Many of the areas most likely to be culled are not particularly pretty. Rather than use architectural merit as a criterion, conservationists are arguing on behalf of structures that hold a “collective memory”. But that can be tricky, especially for endangered buildings such as the old central prison, a place whose traditional use is not universally recalled with fondness.

In the past, sentimental objections to demolition could be brushed aside. Now the era of easy redevelopment may be over. It is true that, despite a period of public “venting”, and even a debate in the city's legislature, Queen's Pier is almost certainly a goner. “We cannot afford heritage preservation if we do not preserve our economic sustainability,” says the chief executive, Donald Tsang Yam-kuen. But there is new pressure, not just for retaining what Hong Kong was, but also for restraining what it might become.

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Thailand's film industry

Royal gala performances

Feb 1st 2007 | BANGKOK
From The Economist print edition

The army and the monarchy are box-office moneyspinners

IF THE secret of success in the cinema is to anticipate the popular mood, Thailand's film industry should be feeling pretty chuffed. It seems to have foreseen, even before last September's royally endorsed military coup, that the army and the monarchy were about to move into the centre of the action.

The bloodless putsch, toppling an elected prime minister, Thaksin Shinawatra, delighted many Bangkok residents, who turned out in droves to have their photographs taken beaming beside the soldiers on the streets. Less than two months later, the film industry scored a surprise hit with “Khao Chon Kai”, a teenage comedy that trumped the latest James Bond escapade, “Casino Royale”, at the box-office. Then in January “The Legend of King Naresuan” set a new record for the Thai box-office, taking 120m baht ($3.4m) in its first four days, despite a shortage of prints of the film and, at three hours, a gruelling running time.

A warrior-king to warm the junta's heart

The Naresuan trilogy, whose second episode opens on February 15th, took four years to make and is, at 700m baht, the most expensive film ever made in Thailand. Foreign films may dominate multiplex schedules, but there's nothing like a local blockbuster to pack the house. Thailand's cinema industry is forecast to expand by 10% this year to 5.5 billion baht, according to Kasikorn Research Centre, a securities firm.

What unites the two very different cinematic hits—a slapstick comedy and a 16th-century swashbuckler—is their gung-ho patriotism . “Khao Chon Kai” is set in an army boot-camp, where, amid much hilarity, young male recruits become battle-ready soldiers. Men in uniform are in cinematic vogue. “First Flight”, another nationalistic drama about Thailand's first air-force pilots, will be screened at the Cannes film festival this year.

“Naresuan”, directed by Chatrichalerm Yukol, himself a member of the royal family, is an even more overt appeal to national unity after the recent upheavals. Its hero is a revered warrior-king—played by an army captain—who repels the occupying Burmese army and restores national pride. The film-makers pull no punches about their intent: the invitation to the première boasts that the film is “aimed at promoting the feelings of patriotism and gratefulness to the motherland” among Thais. The junta must be delighted.

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Shias and Sunnis

The widening gulf

Feb 1st 2007 | CAIRO
From The Economist print edition

David Simonds

Amid Sunni fears of a growing "Shia arc", tensions between the main Muslim sects are widening, while some governments are exploiting them

ISRAEL and America are stirring conflict between Sunni and Shia Muslims so as to plunder their wealth, declares Iran's president, Mahmoud Ahmadinejad. Israel and America are stoking Sunni fear of Shias to distract from the true cause of Palestine, says the supreme guide of the Muslim Brotherhood, Mehdi Akef. Evidently, there is a meeting of minds between the leader of the most powerful Shia state and the head of the world's most influential Sunni political movement.

On the ground across much of the Middle East, the spectre of *fitna*, or sectarian schism, has rarely loomed larger. This week in Iraq, yet another round of bombs deliberately targeted Shia civilians, killing scores. Shia militias responded by lobbing mortars into Sunni districts and by snatching and executing Sunni men. A series of deadly attacks against Shia mosques in Pakistan added a dozen more victims to the estimated 2,000 killed over 15 years of sporadic sectarian violence. In Lebanon, a row in a college cafeteria snowballed into running street battles between followers of rival Sunni and Shia parties; four were killed. The preacher at a slain Sunni youth's funeral described him as a "martyr to Arabism"—a subtle jibe at the ostensibly "Persian" Shias and their leading party in Lebanon, Hizbullah.

This was the week of Ashura, a Shia festival that commemorates martyrdom and has often proved a tense period in places where Islam's two main sects both reside. Yet communal feelings are rising even where Shias, around 15% of the world's Muslims, have little or no presence. In December, Sudan's authorities closed Iran's stall at a Khartoum book fair after Sunni activists accused it of spreading Shia propaganda. Algerian newspapers say Shia missionaries are inveigling Sunni children to convert. Supporters of Fatah, a secular Palestinian party, have taken to chanting "Shia! Shia!" at backers of the Islamist (and Sunni) Hamas party, in a dig against its strong ties to Iran. In Jordan, villagers turned back pilgrims going to a local Shia shrine. Shias say that last month's attacks by vandals in the American city of Detroit on two Shia community centres and some Shia-owned businesses were sectarian.

Some of the alarm appears to be orchestrated. In the culmination of a month-long barrage of innuendo against Iran in Egypt's state-owned press, a recent editorial in the staid Cairo daily, *al-Ahram*, charged the Islamic Republic with undermining chances for peace in Iraq, Palestine and Lebanon. The goal, it suggested, was to weaken Sunni Arab states so as to realise "Safavid dreams" of Shia expansion, a reference to the 16th-century dynasty that enshrined Shiism as Iran's state religion. Citing unnamed Egyptian officials, the same newspaper floated charges that Iranian intelligence agents were responsible for the kidnap and murder of Egypt's ambassador in Iraq in July 2005.

A similar campaign has unfolded in Saudi Arabia, where increasingly internet chat sites, several of which are widely believed to be infiltrated by police agents, are rife with spurious tales of Shia perfidy. A typical item affirms that, when told of Sunni fears of a "Shia crescent" spreading across the region, Iran's president said he envisioned not a

crescent but a full moon. While a columnist in one Saudi daily asserted, falsely, that Shias believe they must perform ablutions if they happen to touch an “unclean” Sunni, 38 senior Saudi clerics issued a call to arms in defence of Iraq against the “Crusader-Safavid-Rejectionist plot” that seeks to uproot Sunni Islam.

Such alarmism reflects, to a degree, a desire by the Sunni, American-allied governments of countries such as Egypt and Saudi Arabia to staunch what they see as a rising tide of Iranian influence. The capture of power by Iraq's long-oppressed Shias is perceived as having, for the first time in history, removed the main Arab bulwark against Persian expansion. Much as most loathed Saddam Hussein, the style and timing of his execution, on a day celebrated by Sunnis as their main annual feast, smacked to many of an ugly Shia triumphalism. Iran's wider assumption of leadership for Islamist “resistance” movements, underscored by the electoral success of Hamas and by Hizbullah's spirited fight in last summer's war with Israel, gives Arab leaders even worse jitters.

At the same time, their American ally is demanding support for its policy of boxing in Iran. Unable to lend much material weight to America's efforts, fearful of a negative backlash should America actually strike Iran, and unwilling to be seen as acting in Israel's interest, Arab countries appear to have chosen to exploit sectarian feelings to send a shot across Iran's bows.

With typical circumlocution, King Abdullah of Saudi Arabia recently said as much. “We have advised them not to expose the region to dangers,” he said, declining to name the country to which he referred. “We don't interfere in anyone's affairs, [but] any state which resorts to unwise acts must bear the responsibility in front of the other countries in the region.”

Bark against the arc

The Saudi intent to thwart Iran's regional ambitions is clearest in Lebanon. The kingdom has lent strong financial and diplomatic support to the government of the prime minister, Fouad Siniora, whose coalition of Sunni, Druze and some Christian parties has been deadlocked in a duel with a grouping headed by Hizbullah. But what has squeezed the Shia party most is loss of the stature it recently gained among a wider Arab public. Seen last summer as the vanguard of the struggle against Israel, it is now viewed by many Sunnis as little more than a cat's paw for Iran.

As Iraq's agony has made clear, sectarianism is a dangerous genie. It was with a view to cooling recent excesses that Qatar, a rich Gulf emirate, invited some 400 top Sunni and Shia religious figures to a dialogue last month. In the event, rhetoric at the conference proved embarrassingly hot. Iran's chief delegate, Ayatollah Muhammad Taskhiri, was besieged with accusations. Iran was failing to stop the ethnic cleansing of Baghdad's Sunnis, he was told. It persecuted its own Sunni minority. Its agents were trying to convert Sunnis and spread Shia texts that insult historic figures revered by Sunnis. Why, retorted Shia delegates, did Sunni clerics so rarely condemn the slaughter of Iraq's Shias? And what of the disenfranchised Shia minorities in Sunni countries?

A message from a senior Lebanese Shia cleric, Muhammad Hussein Fadlallah, provided a useful cold shower. If Sunnis and Shias did not cease their wrangling, he said, Muslims would end up turning to secularism as their saviour.

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The Palestinian territories

The Gazafication of the West Bank

Feb 1st 2007 | HEBRON, NABLUS AND RAMALLAH
From The Economist print edition

Despite a fragile truce in Gaza, factional disputes are spreading

NASSER JUMAA blinks sleepily as he sits on the maroon fake-leather sofa in his downtown office in Nablus, the biggest town in the West Bank. A legislator from the Fatah movement who used to head the Nablus chapter of its military wing, the al-Aqsa Martyrs' Brigades, he has been up all night, trying to talk his former comrades out of retaliating for attacks by the rival Hamas movement on their brethren in Gaza. “I try to convince them that any rash action will backfire on Fatah,” he says.

To no avail, it seems. A little later the rattle of automatic gunfire fills the street below. Mr Jumaa and Sari Hussein, an al-Aqsa Brigades commander who has joined the conversation, rush to the windows to watch. Mobile phones spread rumours that the Islamists of Hamas started it. Within an hour, some of Mr Hussein's colleagues have kidnapped several men linked to Hamas.

AFP

A Martyr Brigadier in avuncular mood

The Gaza Strip has seen the bulk of the conflict between the two parties since Hamas ousted Fatah from the Palestinian Authority (PA) in a general election last year. Clashes there in the last few days of January killed some 30 people, including several bystanders and children. But now the trouble is seeping into the West Bank. Nablus has seen several tit-for-tat kidnappings in recent weeks. Mr Hussein and his men abducted a Hamas deputy mayor after Hamas forces attacked a Fatah commander in Gaza; they also captured a dozen young men who, Mr Hussein says, confessed that they had been training to join Hamas's “Executive Force”.

Hamas's men are more disciplined than Fatah's: the al-Aqsa Brigades are little more than bands of brigands united only by their hatred of Hamas. (Though Fatah condemned the atrocity, an al-Aqsa cell claimed joint responsibility for this week's killing of three Israelis in a bakery in Eilat, the first suicide-bombing inside Israel for nine months.) But Hamas is much weaker in the West Bank than in Gaza, where, in addition to its ordinary militiamen, it has created the 3,000-strong Executive Force under the aegis of the PA—illegally, insists Mahmoud Abbas (Abu Mazen), the Palestinian president. Mr Hussein says he is only trying to stop Hamas from creating such a force in Nablus because “we're against moving the conflict between the parties from Gaza to Nablus”.

The result, of course, is to do precisely that. And the West Bank is starting to resemble Gaza in another way too. As the PA crumbles under fratricidal conflict and the pressure of foreign economic sanctions, the lawlessness has prompted the powerful Palestinian clans (which are not generally loyal to any one party) to see to their own security. Nablus's Dweikat clan recently posted flyers warning that it will retaliate for any attacks on members of the extended family, and has drawn up a list of young armed men that it can call on.

That is a recipe for something nasty. A clan like the Dweikats, with 30,000 members, can be a militia in itself. Clan feuds now drive a lot of the seemingly political fighting in Gaza, and they seem to be intensifying in the West Bank too. Aid workers in Hebron, the main town in the southern bit of the West Bank, say that political clashes there are still rare but arms prices have rocketed, as people buy more guns to protect themselves. In December the police shooting of a teenager prompted his relatives to burn down the police station and kidnap several officers, whose own families then sent in reinforcements, leading to a stand-off that took a week and the intervention of presidential troops to end.

How to defuse things? The two sides have been trying to agree on a unity government for months. After this week's deaths, they accepted an invitation from the Saudi government to hold talks in Mecca. But each accuses the other of sabotaging the deal. And while Fatah says that Hamas has to take its Executive Force off the streets, Hamas men typically accuse not all of Fatah but Muhammad Dahlan, a former security chief in Gaza, of stirring up all the trouble; he was recently appointed by Mr Abbas to shake up both Fatah and the security services loyal to it.

When that was put to him, Mr Dahlan shrugged it off: “If someone in Hamas gets the flu, I'm the reason.” But, he

said, in a surprising show of bravado, “I don't care what Fatah or Abu Mazen says in this regard: if Hamas kills someone from Fatah, I will confront them.” Mr Hussein denies he is taking orders from anyone, Mr Dahlan included; but, he says, “we follow the same principle. We cannot stand by.”

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Israel

A miserable lot

Feb 1st 2007 | JERUSALEM
From The Economist print edition

Why Israelis feel their country is suffering from a malaise

FROM time to time, regular visitors to Israel comment that the people who live there have lost their usually insatiable appetite for talking politics. It last happened in 2002, when the waves of suicide-bombings at the height of the second Palestinian *intifada* shocked Israelis into numbness. Now it is happening again.

As in 2002, Israel feels itself to be facing new threats. The collapse of the Palestinian Authority into factional fighting (see article) offers no reliable partner for a peace deal. Iran's pursuit of a nuclear capability creates a potential existential threat. The recent war against the guerrillas of Hizbullah in Lebanon highlighted the shortcomings of the mighty Israeli army in this new kind of warfare.

But as Ari Shavit, a columnist for the liberal daily, *Haaretz*, wrote last autumn, Israel now faces an "intra-Israeli threat". The prime minister, Ehud Olmert, is under investigation for allegations ranging from dishonest property trading to trying improperly to influence the privatisation of a bank. The finance minister is being probed for embezzlement, the tax-authority head for fraud. The president faces multiple charges of rape. This week a former justice minister was convicted of forcibly kissing a young woman soldier, which could land him in jail for up to three years. The army chief of staff has resigned over the Lebanon war; this month a commission of inquiry is set to shine a harsh light on the performance of army and government.

Mr Olmert's plan to pull settlements out of the West Bank unilaterally to make way for a Palestinian state, on which he was elected less than a year ago, is dead for now, but he has no other programme. The angst-ridden newspaper commentariat throws around words like "rudderless", "corrupt", "wretched" and "vacuum". And in this vacuum, one of the most popular public figures is not a politician but Arkady Gaydamak, a populist billionaire who spreads his money around like water and unashamedly proclaims his desire to be a kingmaker behind the scenes.

In such straits, politicians are sometimes open to new ideas. Some intellectuals who favour peace talks with Syria as an alternative to the "Palestinian track" are calling on the government to give it a try. Mr Olmert, however, brought the right-wing nationalist Yisrael Beiteinu party into his coalition last autumn, which shields the government from collapse but also blocks serious pro-peace moves.

What makes for general gloom is that no obvious alternative is in sight. If elections were held now, according to a poll this week for the Ynet news website, Mr Olmert's Kadima party and Labour, its coalition partner, would each collapse to nine Knesset seats from 29 and 18 (out of 120) now. The right-wing Likud, led by Binyamin Netanyahu, would jump from 12 seats to 32. However, it is far from clear what programme he would offer instead.

A Labour leadership battle in May could bring back Ehud Barak, the prime minister who led Israel into the ill-fated Camp David talks in 2000 and the second *intifada*. He may have matured since then; but a prospective rerun of the 1999 race between him and Mr Netanyahu gives many an uncomfortable feeling of déjà vu.

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Lake Victoria

Woebegone

Feb 1st 2007 | ENTEBBE AND KISUMU
From The Economist print edition

One of Africa's greatest natural resources needs saving

ROMANTICS in the movement to weld east Africa into some kind of union have long seen Lake Victoria as their watery bond, joining Uganda, Tanzania and Kenya in perpetual amity. But the sickly condition of the lake and the broken-down towns littering its shore show why that remains a pipedream, no matter how hard Uganda's president, Yoweri Museveni, and others promote it. If the trio of countries cannot take care of so vital a common resource, what hope for managing a common economy?

Lake Victoria is the second-largest freshwater lake in the world, after Lake Superior in north America. Locals think of it as a sea. In fact, as conservationists often point out, its size is misleading. The lake is shallow: its average depth is 40 metres (131 feet), against 147 for Lake Superior and 758 for Russia's Lake Baikal.

Its ecology is fragile. Most of its many ills are made worse by the increasing number of people who live around it. Perhaps 30m people depend on its water and fish. But the level is down, which some blame on the draw through Uganda's hydroelectric turbines churning water into the Nile. Plentiful rains have raised the lake's level by 60cm since November, but rains bring silting, and the muddy streams coursing in can be thick with fertilisers, raw sewage and other pollutants. The result is a blooming of blue-green algae and rafts of noxious water hyacinth that complicate navigation, deoxygenate the water and kill fish.

This threatens what has become, in effect, the world's largest fish pond. Estimates of the value of the annual catch range from $300m to $590m, most of it Nile perch introduced commercially. The East African Community, which aims for a future union, has institutions to promote sustainable fishing that have improved the monitoring of fish stocks. The number of fishermen has risen fast in recent years.

Climatologists are unsure what effect, if any, climate change may have on water levels. Some think the lake may shrink to its lowest ever. That worries Egypt, which depends on the White Nile's waters, though a lot more comes from the Blue Nile, which rises in Ethiopia. Colonial-era treaties guarantee that the bulk of the flow goes to Sudan and Egypt, which has inspectors along Uganda's stretch of the Nile to check for siphoning off.

Egypt says it wants a better deal with all Nile-basin countries, including Burundi, Congo, Ethiopia and Rwanda. A recent meeting in Uganda's lakeside town, Entebbe, went some way towards that. But it is unclear whether good ideas, such as Egypt's advising on how Lake Victorians could exploit the pond better in return for a guaranteed flow, will work in practice.

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Nigeria

Sharia lite

Feb 1st 2007 | KANO
From The Economist print edition

Moderation from Nigeria's Islamist state governments

WITH some 140m people, Nigeria is not only Africa's most populous country, but also the only one with almost equal numbers of Muslims and Christians. That is one reason why it is a federation, with 36 states enjoying a high degree of independence from the central government. One consequence of that independence has been the implementation, since 1999, of *sharia* law in the north's 12 predominantly Muslim states.

The Islamist revival began in the 1980s, as young Muslims radicalised by the Iranian revolution returned to found their own mosques. Official mosques were sometimes attacked. The new Islamism filled a gap left by the near-collapse of local and federal services, from road upkeep to education, at a time of dreadful mismanagement. The new Muslim groups stepped into the breach, just as evangelical and pentecostal churches did in the mainly Christian south.

The declaration of *sharia* law was presented as an attempt to restore morality and integrity in a corrupt land. But alongside it came what Sherba Garba, a former Muslim and now a member of the general council of the Evangelical Churches of West Africa, describes as “very discriminatory” policies. Christians, he says, cannot get land in Kano state on which to build churches; there are no state-funded schools for Christians. Thousands have died in clashes between Muslims and Christians. In Dutse, capital of Jigawa state, 16 churches were burnt down and thousands of people made homeless in rioting last autumn.

But things may be changing for the better. Some of the Islamist state governments in the north have been responding to pressure for change from their own people by implementing policies that are based on *sharia* law, but which even America and Britain can support. An official in Kano state says a “more pragmatic and realistic” course is being charted to reconcile Muslim and Western values.

Education offers the sharpest example of the new approach. More and more children in Kano are being sent by their parents to private “Islamiya integrated schools”. Unlike state-run Koranic ones, where the curriculum is devoted just to the Koran and Arabic studies, the integrated schools, which are subsidised by the state government, offer a broader curriculum, including English, maths, basic science, health education, handwriting and the local Hausa language. Many, unusually, take an equal number of boys and girls.

The American development agency, USAID, likes the integrated schools' emphasis on educating girls and their attempt to reconcile Muslim and Western education. It now helps fund one of the schools. Umar Sanifagge, one of Kano state's two *sharia* law commissioners, accepts that these schools are “coming at the right time...we have to catch up with modernity and globalisation.”

Kano's *A Daidaita Sahu* programme, which literally means “straighten your rows” (in the manner of worshippers in a mosque), also seeks what it calls “societal reorientation” through educational pamphlets and television programmes dealing with problems such as pollution, petty crime and drugs. People are encouraged, for instance, to recycle the plastic water-bags that pile up in the streets.

The programme's director, Bala Muhammad, says it is successful because it is rooted in the same *sharia* law the state introduced in 1999; indeed, the *sharia* law commissioners sit on his board. And now Britain's aid ministry, noting the programme's declared intention to boost women's rights and reduce poverty, is thinking of helping to promote it too.

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Africa on film

The continent's celluloid moment

Feb 1st 2007
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Lights! Decapitation! Action!

AP

White and black against global evil

SUDDENLY, it seems, Hollywood cannot get enough of Africa. The past year or so has seen the release of a clutch of films set in Africa, all with big stars, big production values—and, unusually, big ideas.

First, in 2005, there was “Lord of War”, starring Nicholas Cage as an arms-dealer in Liberia. Then came “The Constant Gardener”, with its duplicitous drugs companies and deceitful diplomats. Recent films include “The Last King of Scotland”, about Uganda's psychopathic dictator, Idi Amin, and lastly “Blood Diamond”, a story of child soldiers and conflict diamonds (those that help fuel wars) set against the backdrop of Sierra Leone's civil war in the 1990s. Starring Leonardo DiCaprio, it has made the biggest stir, and is in the running for several Oscars at this month's awards ceremony. And before all of these, in 2004, was “Hotel Rwanda”, about the Rwandan genocide of ten years before.

These films are not the feel-good productions that Americans and Britons tend to churn out. They are gritty thrillers immersing viewers in all the nastier aspects of life in today's Africa. Filmed in refugee camps, slums and hospitals rather than out on safari, they make the aristocratic, white world and luscious landscapes of Sydney Pollack's “Out of Africa” look quaint by comparison.

But that was a generation ago. Directors now go to Africa to find stories about arms-trading, genocide, famine and corporate wrongdoing that have filled the hearts and minds of a new generation of Westerners reared on Live Aid and anti-globalisation protests. Instead of old-style product-placement, the new films specialise in NGO-placement.

“Blood Diamond” hails Global Witness, a small British charity that first publicised the ill-effects of conflict diamonds, and the UN's World Food Programme (WFP), which also featured in “The Constant Gardener”. The WFP's spokesman says “it is wonderful publicity”—and even better since the stars now get involved in the issues themselves.

However, this happy new synergy between audience, issues and movie-makers only goes so far. The main protagonists in most of these films are white, so they are still principally about the white Westerner's experience of Africa—just as in “Out of Africa”. Edward Zwick, the director of “Blood Diamond”, argues that it would be “disingenuous” to pretend that he could have got the same financial backing and publicity if he had tried to make a film with a black storyline and a black star instead of one centring on a white mercenary and a (pretty) white female journalist. Hollywood's parameters have expanded a bit, but they are still there.

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France's race for the presidency

Sarko embraces the Anglo-Saxons

Feb 1st 2007 | LONDON
From The Economist print edition

AFP

The centre-right candidate takes a calculated risk in London

Get article background

GIANT screens behind the stage depicted a tranquil French countryside. The audience sang the “Marseillaise”. But the location was London—a former fish market in the City—where one of France's leading candidates for this spring's presidential election, Nicolas Sarkozy, this week took his campaign, calling the British capital “one of the biggest French cities”.

Mr Sarkozy's audacious rally, in the heart of a foreign country, was designed for London's French population, which is thought to be at least 300,000-strong. Many of the audience, holding up their mobile phones to record pictures of the celebrity-candidate, had stepped straight from the nearby international banks. Such were the crowds that some 1,000 invitees were shut out in the street. Mr Sarkozy's message to the 2,000 squeezed inside was partly a call to vote to revive France's “blocked society” that they had left behind “in desperation”, and partly a call to “come home” and “make France a great nation”.

Mr Sarkozy's London trip, though, carried a wider symbolism. He dropped in for lunch with Britain's prime minister, Tony Blair, and took television cameras with him to a London job centre. The point was plain: the British have made their economy work, and I could do the same.

In any other country, this message might seem banal. France's unemployment rate is 8.6%, compared with 5.5% in Britain, and has not dipped below 8% for nearly 25 years. Britain's lower-taxed, less regulated economy has helped to encourage entrepreneurship and dynamism, and its GDP per head has overtaken that of France. Pragmatism suggests that there might be a lesson in there somewhere.

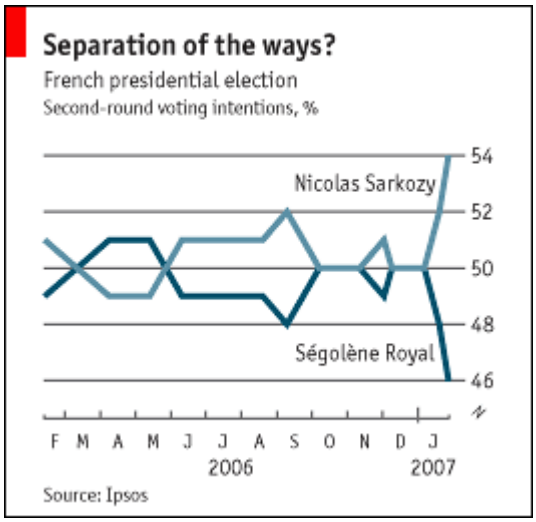
Yet, in France, too close an association with *les Anglo-Saxons* is usually seen as a liability, and not just because of differences over Iraq. On the right, as well as the left, there is a lingering suspicion of what is regarded as a heartless laissez-faire economy, in which low unemployment disguises a world of precarious “McJobs”. President Jacques Chirac once said that there was “nothing to envy nor to copy” in the British model. “Britain's economy may have grown faster,” sniffs one senior Socialist, “but it is a deeply unequal society with millions in poverty.”

Moreover, his London trip was not the first time that Mr Sarkozy has tried to seduce the French with an Anglo-Saxon foray. In September he jetted to Washington to see President Bush. This provoked consternation and derision in equal measure from the Socialist Party, and has fed its election campaign ever since. Eric Besson, economic adviser to Ségolène Royal, the Socialist presidential candidate, recently called Mr Sarkozy “an American neo-conservative with a French passport”.

So why does Mr Sarkozy pursue this strategy? One answer is that he is trying to model himself as an alternative to the president he now serves. Although he says he will leave the interior ministry before the official campaign kicks off in April, he remains for now a member of an unpopular government. Hanging out with Anglo-American friends shows how different he is. On the steps of Downing Street this week, Mr Sarkozy carefully placed an affectionate hand on Mr Blair's shoulder as they said goodbye.

A second explanation is that Mr Sarkozy believes that French antipathy to Anglo-Saxons is an elitist indulgence not shared by the French at large. As he told a Washington audience: “The truth is that the French listen to Madonna, just as they used to love listening to Elvis and Sinatra... And all French parents dream of sending their child to an American university.” His conclusion was that “the virulence of the press and a portion of the French elites against the United States reflects a certain envy of your brilliant success.”

He has a point. If the French are so scornful about the low-paid jobs in London, why do so many young French people head across the Channel to fill them? Jobs may be less secure, but they are more plentiful. The biggest cheer during his London rally this week came when he chastised French society for not rewarding effort and risk-taking. In other words, if the French do secretly admire the American and British record on employment, they may reward a pragmatic electoral message that disregards ideology.



All the same, it carries a risk. Indeed, Mr Sarkozy is seeking to temper his liberal message with speeches about “the France that suffers”. He is treading a perilous line between promising to shake things up and reassuring voters that he will protect them.

For now, the risk seems to be paying off. One poll, by Ipsos, this week gave him 54% of the vote in a run-off against 46% for Ms Royal—the widest gap of any poll taken since Mr Sarkozy got his party's nomination on January 14th. Ms Royal has been damaged by a succession of foreign-policy gaffes in recent weeks, which have lent her campaign an air of amateurism. She badly needs to appear both competent and concrete if she is to reverse her slide—and close off the space for the political gymnastics of the daring Mr Sarkozy.

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France and tobacco

Smoking and the 35-hour week

Feb 1st 2007 | PARIS
From The Economist print edition

The workers' right to inhale, but on whose time?

PEDESTRIANS in Paris are used to dodging *déjections canines* (dog-poop), but these days a new hazard is blocking the French capital's pavements: smokers fleeing the country's new anti-tobacco law. On February 1st France followed a European trend by making it illegal to smoke in offices, so forcing staff out into the streets to light up. The country's strict working-time rules, though, add a particular French twist: should smoking breaks be counted as part of the 35-hour week?

France's legendary 35-hour regulations, introduced in 2000-02, prompt a constant stream of labour-court rulings. Late last year, for instance, the Paris Court of Appeal ruled against Euro Disney, upholding a claim by employees that the time they spent in full costume travelling between the dressing room and their spot inside the theme park should count as part of their working hours. Every minute counts—and is counted. When in 2005 the government allowed employers to decide whether to work on a public holiday, the SNCF, the public railway, decided to maintain the paid day off—but in return for staff working an extra one minute and 52 seconds each day.

The new anti-smoking rules do not specify how to treat time spent on a *pause cigarette*. But they do make it all but impossible for France's 15m smokers to light up in or near an office building—as well as schools, hospitals, public transport, and, from 2008, bars, hotels and restaurants. In principle, companies can install "*fumoirs*", airtight rooms for smokers, but these cannot be over 35 square metres (377 square feet), must have powerful ventilation, and even the cleaner is not allowed in until an hour after the last smoker has left. So the street is the last refuge, and employers have been in delicate negotiations over how to count pavement time. To the outrage of some, several companies have decided to clock out staff as they leave the building for a smoke, and deduct the time from working hours.

It is not only the labour lawyers who are getting ready for the fall-out from the revolutionary new law. Bertrand Delanoë, the capital's Socialist mayor, recently unveiled a new cleanliness plan for Paris, which included measures to combat the growing number of cigarette butts strewn across the pavements. One idea is to install municipal ashtrays in public places. Another is to fine companies whose staff chuck their cigarette ends onto the street. Hounded smokers are horrified by all this, and would doubtless take to the streets—if, that is, they were not there already.

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German anti-terrorism

A complicated business

Feb 1st 2007 | BERLIN
From The Economist print edition

Frank-Walter Steinmeier fights for his reputation and perhaps his job

THE complications of America's "war on terror" continue to bedevil German politics. Did ministers turn a blind eye to the "extraordinary rendition" by the CIA of suspected terrorists, including Khaled al-Masri, a German citizen of Lebanese descent who was seized in Macedonia and then imprisoned in Afghanistan for five months before being released without charges? Did they also let Murat Kurnaz, a German-born Turk, languish for four years in Guantánamo Bay—the American holding centre for suspected terrorists—even though America was ready to release him after one year?

This week a court in Munich issued an arrest warrant for 13 unnamed members of a CIA team said to have abducted Mr al-Masri in late 2003. Soon, a parliamentary committee investigating the exact nature of Germany's collaboration with America after September 11th 2001 will hear evidence from Frank-Walter Steinmeier, Germany's foreign minister. He will have much to explain—and might even be embarrassed out of office.

The reason is that Mr Steinmeier was Chancellor Gerhard Schröder's *chef de cabinet* between 1999 and 2005. In October 2001, just after the World Trade Centre attacks, 19-year-old Mr Kurnaz—who grew up in Bremen but as a Turkish national—flew to Pakistan. He was picked up by Pakistani security forces and passed to the Americans, who held him in Afghanistan, where he was allegedly hit by German soldiers and tortured by American ones. By February he was in Guantánamo Bay.

Three German security officers interrogated him there in September 2002, with a CIA agent listening in; they judged him harmless, with "no innate religious ideology". Turkish officials visited Mr Kurnaz too, but the government had five other citizens in Guantánamo to worry about. The Germans dithered. A sticking point may have been a proposal, which was rejected, that Mr Kurnaz should be used in Germany to inform on Islamist extremists.

The case was handled in Berlin at regular meetings of the Präsidentenlage, a council comprising top foreign, interior and justice ministry officials and the heads of three security agencies; it was often chaired by Mr Steinmeier. The Präsidentenlage reacted strangely in late 2002 to information that America might soon free its first batch of Guantánamo prisoners: it tried to cancel Mr Kurnaz's right of entry to Germany, hoping that he would be sent to Turkey. Then, in early 2003, the Americans appeared to have second thoughts about Mr Kurnaz, intimating that he was not being totally honest about his activities in Pakistan. On this pretext, but on no prima facie evidence, it seems the German government was prepared to let Mr Kurnaz languish in Guantánamo—an institution seen by most Germans as an affront to human rights and international justice—rather than bring him home to Germany.

Mr Kurnaz was eventually freed in August 2006 through the efforts of the new coalition government; he was the last European to leave, says his lawyer. Back in Germany he was watched for a while but the only criminal investigation had been dropped back in October 2002. The affair flared recently when Mr Kurnaz gave graphic evidence to the parliamentary committee of his mistreatment and torture in captivity. So how will Mr Steinmeier explain himself? "I would decide no differently today," he told the weekly *Der Spiegel*. "They were very political decisions," he added, in a remark pounced on by many as an admission that the rights of an innocent man were not uppermost in the minds of Mr Steinmeier and his colleagues four years ago. Those colleagues included Joschka Fischer and Otto Schily, the foreign and interior ministers of the time, both now safely in retirement.

Bernd Rosenkranz, a civil-rights lawyer, last week filed a complaint against Mr Steinmeier and three other members of the Präsidentenlage, alleging that their actions deprived Mr Kurnaz of his freedom and caused him bodily harm.

Mr Steinmeier, meanwhile, is reckoned a good foreign minister. Losing him would hardly help Germany's much-ballyhooed six-month presidency of the European Union and 12-month presidency of the G8 industrial nations.

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Italy's reform programme

Two steps forward

Feb 1st 2007 | ROME
From The Economist print edition

The need to compromise still frustrates the need to liberalise

THEY lit the blue touch-paper; everyone stood back—and the bang was barely audible. So much, the pessimists may think, for yet another attempt by Italy's politicians to liberalise the country's red-tape-bound economy. On January 25th Romano Prodi's centre-left cabinet agreed to try for a second time within a year to make life easier for the consumer, whether buying petrol or getting a haircut.

More competition and less regulation are sorely needed in Italy. A shortage of the former and a glut of the latter are important reasons why the country has underperformed the rest of the European Union since the mid-1990s. An initial, tentative stab at liberalisation last July provoked a vigorous and at times violent response from the country's taxi-drivers. This new attempt moved Italy's petrol retailers to threaten a series of two-day strikes that could be immensely disruptive to a society with Europe's highest rate of car ownership. The first stoppage is due on February 7th and 8th.

But the latest reforms also seem to be popular. One consumer group estimated that they could save the average household €550 ($713) a year. Some 86% of people polled by the Repubblica.It website said they thought the changes “very” or “quite” important.

Not all, however, count as real liberalisations. Many in the package assembled by Pierluigi Bersani, the economic-development minister, are actually consumer-protection measures, and it was they that won the widest endorsement.

One such change stops telephone companies from charging extra to customers using pre-paid phone cards. Another forces airlines to advertise the full cost of tickets. Food manufacturers will be made to display prominent “sell by” dates. Banks will be prevented from penalising clients who pay off their mortgages early. And Italy's legendarily erratic postal service will have to offer compensation for delayed or lost letters.

In contrast, it is the genuinely liberalising measures that seem to have stirred the greatest misgivings among the public (though they too won majority backing in the Repubblica.It poll). Perhaps the most far-reaching measure is one allowing Italians to set up businesses in just a week (an EU study found that in 2002 it took 35 days to set up a company in Italy, compared with seven in Britain). Others are aimed mainly at the retail sector.

Until now, for example, anyone opening a petrol station, a cinema or a newsstand could not do so within an officially-prescribed minimum distance from the next one. Those rules will be abolished, leaving supermarkets free to sell petrol and petrol stations freer to sell products other than petrol. Anyone will be entitled to sell newspapers. Hairdressers will be able to open salons wherever they please and keep them open as long as they like (they now close on Mondays). Estate agents will no longer have to be listed on an official register. People setting up cleaning companies will no longer have to show the necessary “cultural requirements”, while foreigners will be eligible to guide tourists (though they will still have either to pass an Italian exam or possess a relevant university degree).

All of which is nice for the consumer. But can such a ragbag of measures bring much new dynamism to the economy? Francesco Rutelli, one of Mr Prodi's deputies and leader of the moderate wing of his coalition, thinks not. It was, he told associates, “ridiculous” to be worrying about hairdressers and petrol retailers while there was scarcely any competition in key sectors such as energy and transport.

He has a point. But Mr Bersani is a member of the Democrats of the Left, the heirs of Italy's mighty Communist Party. Unsurprisingly, he fought shy of anything that might bring him into conflict with the trade unions. In the cabinet meeting called to review Mr Bersani's bill, Mr Rutelli tabled a rival one. It was not adopted, but the package that ultimately emerged does bear some traces of Mr Rutelli's influence.

One is a provision allowing mortgages to be switched between lenders. A second opens inter-regional coach services to competition. Most important of all, Mr Rutelli, who has staked his credibility on securing a more vigorous approach to liberalisation, obtained a commitment that a bill will soon be drawn up to hive off Italy's gas supply network, currently operated by the country's energy megalith, ENI.

The verdict of Italy's few long-standing economic liberals was that Mr Bersani's second package was a step in the right direction, but a limited one. “If we were Milton Friedman's [kind of] government, we'd do more,” says Emma Bonino, the Europe minister. “But we're not. This is a government that looks for compromise.”

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Ireland's pre-election politics

The sinner absolved

Feb 1st 2007 | DUBLIN
From The Economist print edition

Sweetening the cake, little by little, is to the voters' taste

FEW Irish politicians can match Bertie Ahern in the delicate art of political timing, at least in wooing and winning voters well in advance of a general election which, as taoiseach (prime minister) he must call by June—though May is the expected date. And he is doing so by orchestrating a monthly stream of "good news" events, while exploiting them to good political effect. These are designed to raise his profile, which is never very low, and also the popularity of his centre-right coalition, which is rising steadily. As a result, Mr Ahern is peaking in the polls at the right time, just as his rivals show signs of floundering.

In December, for example, he presided over a generous, yet fiscally responsible, budget. This combined large tax reductions with a 5% real increase in spending—but, even so, a budget surplus is forecast by year-end. In the ten years that Mr Ahern has led his Fianna Fail party in a coalition with the Progressive Democrats, a small liberal party, his government has only once incurred a budget deficit.

On January 23rd Mr Ahern launched a second electoral sweetener: a €184 billion ($238 billion) national-development plan for the economy over the next seven years. This also includes a likely €1.2 billion for projects in Northern Ireland: an economic dimension of the peace process. The plan, which will tackle infrastructure deficits in areas such as roads and housing, will be funded almost entirely from domestic resources, with little reliance, unlike previously, on support from the European Union. The economic blueprint envisages a continuation of the boom, though at a more moderate pace. Since 2000 the Irish economy has grown at an average of 5%, or more than double the EU rate, and enjoys virtual full employment, with one in ten workers now a foreigner.

Soon, Mr Ahern may well have further reason to celebrate. On January 28th in Dublin, Sinn Fein took an historic decision to recognise the Northern Ireland police force. That move may lead to the restoration of a devolved government in Belfast by the end of March. If that happens, it would be a vindication of the painstaking efforts of both the taoiseach and the British prime minister, Tony Blair, to secure the full implementation of the "Good Friday" peace agreement for Northern Ireland.

In April, a government-subsidised savings scheme matures. Investors will find themselves with an estimated €10 billion at their disposal, which is certain to raise consumer confidence ahead of an imminent general election.

Yet just four months ago, with the disclosure of a financial scandal, Mr Ahern's future was looking bleak and his party's re-election prospects were in the balance. As minister of finance in the early 1990s, he had received financial gifts and loans from friends and businessmen and had failed to declare them publicly. In October he said that he had received the payments, the details of which he found hard to remember or explain, while experiencing some difficulties in his personal life: he was involved in proceedings for a marital separation.

Mr Ahern's problems presented the alternative government on offer to the voters—a centre-left coalition of Fine Gael and Labour—with its best ever opportunity to gain at his expense. They bungled their chance: the two parties hesitated, and failed to table a parliamentary vote of no confidence in his leadership. Mr Ahern, whom his mentor, the late and now infamous former taoiseach, Charles Haughey, once described as "the most skilful, the most devious, the most cunning of them all", later apologised to the nation for his unacceptable behaviour. And the public, to judge by the subsequent opinion polls, may have hated the sin but they have absolved the sinner.

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Charlemagne

Coalitions for the willing

Feb 1st 2007
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"Multi-speed Europe" is making a comeback, along with the constitution

DISCUSSING the European constitution at a recent informal meeting, a high-ranking German politician suddenly veered off topic and onto the merits (and drawbacks) of "three-speed Europe", the idea that the European Union might adopt different categories of membership, with gradations of responsibility. The change in direction was, to say the least, somewhat unexpected: such an idea is very different from the constitution, and getting that document passed is the German government's foreign-policy priority.

Two weeks later, it happened again. This time, the Spanish foreign minister, opening a conference of countries that have ratified the constitution, discoursed on "mechanisms of differentiated integration"—EU jargon for two-speed Europe.

Talk of two-speed, three-speed, multi-speed or any other bicycle gearing mechanism is strange now, when all eyes are supposed to be on ratifying the constitution. The constitution is a step everyone takes together. It fits the famous definition of British cabinet responsibility in Sellar and Yeatman's spoof history "1066 and All That": it does not matter what politicians say so long as they all speak at once. Notions of multi-speed Europe are the opposite. They imply that some countries could push ahead, others could hold back and the union as a whole would evolve from a monolithic one-size-fits-all block into a club in which membership would mean different things to different people.

At the moment, it is best to regard such chatter as a threat. Supporters of the constitution are saying to opponents: you had better ratify this document or we will press ahead and create an inner circle, leaving you outside. Then you'll be sorry.

Actually, they probably wouldn't be, because this isn't much of a threat. Talk of "core Europe", and various other slogans advanced by, amongst others, Jacques Delors and Valéry Giscard d'Estaing, is almost as old as the institutions of Europe—and has never come to anything. It poses huge institutional problems (what would be the relationship between the inner core and the EU itself?) and the Germans have never been very keen because they want to anchor their country in Europe as a whole, not in a self-selected bit of it. The idea would be less plausible now, in an EU of 27, since an inner circle around France and Germany would not have the same impact as it would have done in a Europe of 12 (even assuming such a group could be established).

Still, plausible or not, politicians will soon be paying more attention to multiple speeds and all that. If the constitution fails, demands for an inner circle will grow in countries such as Belgium, whose prime minister wants a United States of Europe based on the euro. The same thing might happen even if the constitution passes in the form of a stripped-down treaty that tinkers with the EU's institutions but lacks grand gestures of integration.

Pressure for closer union through multiple speeds might seem, as Sellar and Yeatman would have put it, A Bad Thing: it suggests the EU will never reach a constitutional settlement. In fact, a multi-speed Europe, properly conceived, could reduce some of the tensions inherent in countries' differing appetites for integration. It would be A Good Thing. To see how, forgive a quick dip into the turbid waters of EU theology.

There are 57 varieties of multi-speed Europe but only two basic types. In the first, an elite group of countries would sign up to closer co-operation right across the board, probably by establishing a new organisation parallel to the EU. They would form a club within the club. The rest would co-operate on only a few things, forming an outer ring or two. This is variously called “core Europe”, “concentric circles” or “two-speed Europe”.

In the other type, all countries sign up to a basic set of rules (in practice, the single market). Smaller groups then volunteer to co-operate in specific areas—policing, say, or foreign policy. There would be many such groups, with overlapping memberships. This idea might be dubbed “coalitions of the willing” (to borrow Donald Rumsfeld's phrase) but suffers under horrible labels like “enhanced co-operation” and “variable geometry”.

Whatever you call it, the latter idea—unlike the former—has much to recommend it. For one thing, it works. We know this because while the EU likes to pretend everyone will eventually sign up for everything, in practice it has developed the euro (legal tender in 13 countries of 27); the Schengen agreement for passport-free travel (15 countries implement this, including three non-EU states); and the arrangement by which Britain, France and Germany speak for everyone in dealing with Iran. In each case—and there are others—pioneers were able to push ahead without precipitating a constitutional crisis with the cautious.

Willing, but not always able

As with anything in life or politics, coalitions of the willing can be good or bad, helpful or horrible, depending on the details. But potentially, the idea would allow countries that wanted more co-operation in controversial areas, such as defence or criminal justice, to move ahead without affecting those who want to retain a national veto in such matters. This would not only be more democratic (why should countries that wish to pool sovereignty be stopped by others, if others are not harmed?). It might also soothe some of the neuralgic objections to enlargement, since new members, such as Turkey, could join a “basic EU” while existing ones experiment with closer co-operation.

“One can only reconcile a deepening of EU integration with enlargement of the EU by allowing some countries to go further,” wrote Jacques Delors in 2000. This multi-speed approach would be a better way of answering some of the genuine problems of the EU than the constitution would provide, and should be adopted instead. As Sellar and Yeatman advised in their mock exam questions: Do not attempt to answer more than one question at a time.

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Terrorist plot

From Baghdad to Birmingham

Feb 1st 2007
From The Economist print edition

AFP

A thwarted conspiracy aimed to divide Muslims into insurgents and collaborators

DURING the three long weeks in 2004 when Britons waited anxiously to hear the fate of Ken Bigley, a Liverpudlian engineer who had been taken hostage by insurgents in Iraq, most could draw solace from the fact that behind him stood a country united in revulsion at the deed. Both the Muslim Council of Britain (MCB) and the more radical Muslim Association of Britain, neither of them fans of British foreign policy, called for his release and condemned his subsequent beheading.

Britain may have escaped a similar horror transposed to homelier climes this week. On January 31st the West Midlands police arrested nine men in the area around Birmingham. Security sources reportedly said the men were plotting to kidnap a young Muslim soldier on leave from duty with the British army in Afghanistan, and to broadcast his execution over the internet. Some reports suggest he was to have been tortured and forced to denounce the army.

More than once before now police have burst into homes and hauled away suspects only to return them later, uncharged. But if such a plot is proven to exist, it marks a disturbing change in the pattern of terrorist attacks in Britain. The London bombings in July 2005 were designed to impress through indiscriminate killing. Choosing this particular fate for this particular victim suggests a different set of aims: driving a wedge between Muslims and punishing those who dare to put country over religious identity.

That such a plot should have been hatched is not surprising. Political abduction and murder in the United Kingdom are not novel. In 1984 Ravindra Mhatre, an official at the Indian consulate in Birmingham, was kidnapped and killed by terrorists in one of the neighbourhoods where police were active this week. Captain Robert Nairac of the Grenadier Guards was abducted and killed by the IRA in Northern Ireland in 1977. Terrorism experts have long given warning that the wars in Iraq and Afghanistan pose a danger of “blowback”—radicalising some British Muslims and inspiring them to use tactics that are common among insurgents there.

Although most British Muslims (and many non-Muslims) oppose the wars in Iraq and Afghanistan, about 330 still wear the uniform. In July last year Lance Corporal Jabron Hashmi, a British citizen born in Pakistan, was killed in Afghanistan, becoming the army's first British Muslim soldier to fall in that arena.

The armed forces are keen to attract more Muslims and deflect criticism that Britain's is a crusading army defiling Muslim lands. The army now allows Muslim soldiers to wear beards and Muslim women to ditch their khaki skirts for more concealing trousers. In January the MCB offered to help the recruitment drive. Some Muslim scholars have even ruled that followers of the Prophet who are killed fighting Britain's wars are still regarded as heroes.

Small numbers of British Muslims are attracted to the ideology of global jihad and it is not easy to predict who

they will be

The raids came at a time of growing concern about Muslim alienation in Britain. This week the Conservative Party's policy group on security, led by (Dame) Pauline Neville-Jones, a former intelligence supremo, gave warning that “a battle is under way for the allegiance of British Muslims between an ideological movement which challenges democratic values and also tries to squeeze out more liberal Islamic traditions, and the values of broader British society.”

New polling data by Populus for Policy Exchange, a think-tank, suggest that young Muslims are far more likely than older ones to sympathise with extreme manifestations of Islam. Some 36% of 16-to-24-year-olds said that conversion from Islam should be punished with death, for example, and 74% said women should wear the veil. Of Muslims over the age of 55, only 19% and 28% respectively felt the same.

Though these figures are cause for concern, they should not inspire panic. Young people are more likely to agree with their elders as they themselves age; and the same poll found that 59% of all Muslims think they have as much or more in common with non-Muslim Britons than with their Muslim brethren abroad. Almost a year after the London bombings, about two-thirds of Britons told pollsters for the Pew Centre in America that they had a favourable view of Muslims. And the Populus poll found that 84% of Muslims think they have been fairly treated in Britain.

The problem is that small numbers of British Muslims are attracted to the ideology of global *jihad* and it is not easy to predict who they will be. Previous plotters have mostly been second-generation immigrants who have sought out radical Islam for themselves. Some have been well educated: Omar Khan Sharif, who carried out a suicide bombing in Israel in 2003, and Omar Sheikh, arrested for his part in the murder of Daniel Pearl in Pakistan, attended prestigious universities in London.

The fact that this plan seemed designed to separate British Muslims into collaborators and insurgents suggests that the wannabe *jihadis* know things are not going entirely their own way. These are the tactics of thugs on the fringe.

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Northern Ireland

Virtual democracy

Feb 1st 2007 | BELFAST
From The Economist print edition

Elections are scheduled for March 7th—maybe

NO SOONER does Northern Ireland negotiate one hurdle on the road to restored self-government than another one appears. On January 28th Sinn Fein's members, who once lauded wholesale violence, pledged their support for the Police Service of Northern Ireland—heir to the hated Royal Ulster Constabulary. Gerry Adams, the party's president, promptly urged victims of crime to seek police help and promised republicans who want to join the force Sinn Fein's blessing.

It all seemed promising for the resumption of legislative business at Stormont, suspended since 2002. This depends on republicans' acceptance of the rule of law, unionists' agreement to share power with their erstwhile enemies, and the willingness of either to take the first big step.

And the good news continued on January 30th, when the International Monitoring Commission said that the IRA had convincingly abandoned terrorism. Seizing the moment, the prime ministers of Britain and Ireland, Tony Blair and Bertie Ahern, announced shortly afterwards that elections for a new assembly would take place on March 7th, leading to a resumption of devolved self-rule on March 26th.

That, at least, is the theory. Whether the elections actually come to pass depends mainly on two men: the Rev Ian Paisley, hardline leader of the Democratic Unionist Party (DUP), and Mr Blair himself.

The 80-year-old Mr Paisley has spent his life harrying other unionists who proposed the slightest compromise with peaceful nationalism, let alone the sort of violent republicanism once carried out by Mr Adams and his IRA subordinates. Many wonder whether he can actually stomach the prospect of leading a new government with Martin McGuinness, a former IRA leader, as deputy first minister. Mr Paisley says that he will “not be found wanting” if the republicans match their fine words with deeds. But he is constantly redefining just what the deeds need to be in order to qualify.

He wants republicans to help finger those who killed Robert McCartney, a Belfast Catholic stabbed to death two years ago in a pub brawl, allegedly by members of the IRA. Mr Adams used to advise anyone with information to speak to lawyers, priests or the victim's family. On January 31st he changed his mind: people should now contact the police, he said. Mr Paisley also thinks republicans should give evidence to clear up the many unsolved IRA murders and hand over their ill-gotten gains from various robberies.

It is unclear why Mr Paisley would participate in the elections if he did not intend to go through with the result. In a sense he stands to lose whichever way he moves. Most of his own followers, including those in his church, hate the idea of power-sharing. Yet there is also some appetite in the DUP for a deal, not least among politicians whose future salaries require one.

In the end much may depend on whether Mr Blair can convince Mr Paisley that this deadline is a deadline. It may well be the last deal Mr Blair can broker, for he leaves office this summer. He talked tough this week, promising to cancel the elections and resume direct rule in earnest if either party looked less than committed. Fine talk—but we've heard its like before.

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The cash-for-honours affair

Now it's a cover-up

Feb 1st 2007
From The Economist print edition

The police raise the stakes

WITH the re-arrest on January 30th of Lord Levy, the Labour Party's chief fundraiser, the police have ratcheted up their investigation into the alleged sale of peerages for cash. On this occasion Lord (Michael) Levy, dubbed by some “Lord Cashpoint”, was detained on suspicion of conspiracy to pervert the course of justice. A fortnight earlier, Ruth Turner, an important member of Tony Blair's staff, was arrested on similar grounds before, like Lord Levy, being released on bail. On January 26th, police interviewed Mr Blair himself for a second time.

The mood in 10 Downing Street is newly miserable, for the police investigation had seemed to be winding down before Christmas. The betting then was that the police had not found enough evidence to justify a prosecution for selling peerages. But charges for failing to declare loans given on soft terms as political contributions did still seem possible.

Even before Miss Turner's arrest, however, there were reports that the police had convinced themselves of a cover-up within Downing Street that was preventing them from getting their hands on evidence they were looking for. Last week it emerged that the police believed a second, “hidden”, Downing Street computer system existed from which crucial emails had been deleted. The prime minister's spokesman denied the allegation.

If the police can show that an attempt to conceal vital evidence has taken place, the consequences for the perpetrators could include prison sentences running to several years. What gives the accusation plausibility is that it is the usual story in cases involving politicians from Watergate to Jeffrey Archer and Jonathan Aitken: it is the cover-up that gets them in the end.

But if their suspicions cannot be proved, Mr Blair and his colleagues will be justified in feeling angry over the way they have been treated. In particular, they say they are shocked by the leaks tracking every twist and turn in the investigation. Downing Street believes that these must have come from the police themselves.

In the meantime, the fallout from the police investigation is helping to make Mr Blair's final months in office more tragic denouement than triumphant farewell. However good Mr Blair is at compartmentalisation, it is hard to believe that the work of the people he most depends upon—such as his chief of staff, Jonathan Powell, whom the police may well interview again any day—has not been affected.

Next week the government is expected to publish a white paper setting out its proposals for reforming the second chamber. Under the circumstances, it would have been understandable if it had decided to end once and for all the practice of parties nominating supporters to the House of Lords. But apparently not.

Under the new plans, half the seats are likely to go to elected peers who will serve a 15-year term. The independent appointments commission will nominate another fifth, striving for a balance of gender, ethnicity and expertise. But political parties will still nominate 30% of the upper house. Old habits of patronage die hard.

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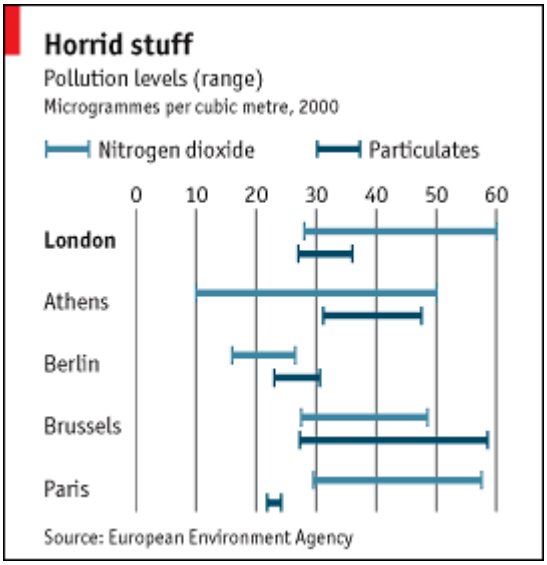
About sponsorship

Air pollution

The Big Smoke

Feb 1st 2007
From The Economist print edition

London tries to clean up its air



COAL fires and pea-souper fogs are a relic of the last century, but London is still one of Britain's least pleasant places to go cycling. The capital's air is the dirtiest in the country and among the worst in western Europe (see chart). Levels of nitrogen dioxide (a toxic chemical that damages the lungs) are above official limits throughout the city, and several areas exceed similar limits on particulate pollution (which may also carry carcinogenic chemicals). Foul air kills about 1,000 Londoners a year, for the most part by exacerbating lung diseases, and recent data suggest that the problem is getting worse.

The main culprit is road transport, especially the diesel-powered variety. Traffic generates around two-thirds of London's fine-particle pollution and 40% of the noxious nitrogen. Inspired by the success of his road-charging scheme in unclogging city-centre roads, Ken Livingstone, the city's mayor, has promised a similar approach to tackle air pollution. He plans to designate almost the entire city as a low-emissions zone (LEZ). Beginning in 2008, a network of automatic cameras would trigger charges of up to £200 ($391) on heavy diesel-powered vehicles (mainly buses and large lorries) that did not meet European emissions standards. In its public consultation on the scheme (which closed on February 2nd), Transport for London (TfL) put the public-health benefits as high as £460m.

Everybody agrees that it would be nicer if the capital's air were more breathable but not everyone thinks that the mayor has the right approach. London First, a business-funded lobbying outfit, points out that the LEZ's cost-benefit ratio is the highest of any project that TfL is currently funding, appearing to fall outside central-government guidelines. That criticism is echoed by the environment department. London First claims that a smaller zone that covered only the city's particularly grimy central areas would be better value for money.

Others worry that, although particulate emissions are thought to be the most harmful sort, other pollutants are not covered. The scheme takes no account of planet-heating carbon dioxide, of which diesel engines tend to emit less than petrol-powered ones. Frank Kelly, an air-quality expert at King's College, London, points out that, although the zone will bring cleaner air overall, many new engine designs obtain their low levels of particulate pollution at the expense of higher outputs of nitrogen dioxide.

The scheme's most striking flaw is that although it will be extended to light vans after 2012 there are no plans to charge private motorists. Officials cite technical difficulties and point out that, individually, cars produce fewer nasties than lorries. But there are far more cars on the roads than heavy goods vehicles, and in aggregate they produce roughly as much atmospheric muck as lorries do. Those in the know whisper that Mr Livingstone is worried that London's motorists—already fed up with high parking charges and an unwanted westward extension of the congestion-charging zone—might rebel if they were to face pollution charges too.

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Public finances

Browned off

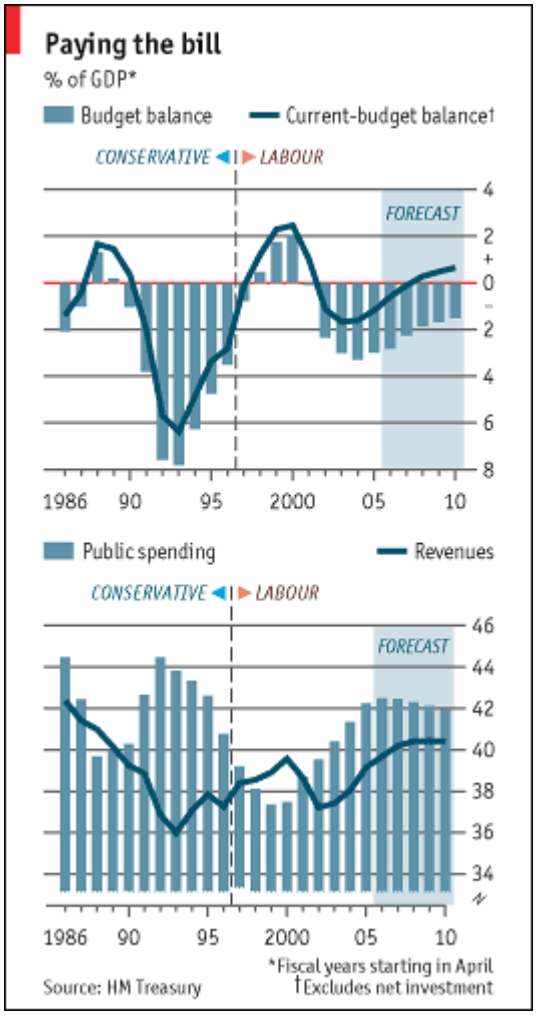
Feb 1st 2007
From The Economist print edition

The chancellor has spent, taxed and borrowed too much

Get article background

GORDON BROWN wrote himself into the history books in 2004 when he became the longest-serving chancellor of the exchequer since William Gladstone over a century ago. But the record that matters for him and the public is not how long he has managed the nation's finances, but how well he has done it. That verdict is now due as Mr Brown, the odds-on favourite to replace Tony Blair as prime minister later this year, prepares to leave the Treasury.

In its annual budgetary review, the Institute for Fiscal Studies (IFS), an independent think-tank, says that the chancellor will leave the public finances stronger than he found them. The IFS contrasts the positions in the current 2006-07 tax year with that of 1996-97. This year's overall budget deficit will be 2.8% of GDP, lower than the 3.5% gap under the Tories in their last year in office (see chart). What is more, a bigger share of Mr Brown's borrowing is financing capital spending. The current-budget deficit, which excludes net investment, will be 0.6% of GDP in 2006-07, compared with 2.8% in 1996-97.



The institute's judgment, based on these two snapshots, seems rather charitable. Mr Brown has certainly done a lot better than the Conservatives did in the early 1990s when a huge hole opened up in the public finances. But they were already on the mend, thanks to painful Tory remedies, by the time Mr Brown took over the Treasury. Furthermore, as the IFS points out, other countries have done better in the past decade. Out of 22 developed economies, 15 reduced their debt and 17 improved their underlying budget balances by more than Britain did between 1996 and 2006.

Mr Brown's chequered record as finance minister is in fact a familiar one. Like so many of his post-war predecessors, both Labour and Conservative, the man from the Scottish manse has played the part of the prodigal son. Now taxpayers are once again having to bail out, if not forgive, an improvident chancellor.

What makes Mr Brown's tenure at the Treasury distinctive is not only its length but also its trajectory. Previous chancellors made the mistake of overspending in haste, only to have to repent later. Mr Brown, a keen student of political history, did not repeat that error. Instead he practised as well as preached prudence, sticking with tough Tory plans to freeze public spending in real terms for two years. Indeed, spending fell from 40.8% of GDP in 1996-97 to a low of 37.1% in 1999-2000. Since tax revenues were unexpectedly strong, the public finances swung into a big surplus around the turn of the century.

The temptation to raid the exchequer's brimming coffers became irresistible. Mr Brown called his budget in 2000 “prudent for a purpose”. The purpose turned out to be an extraordinary sustained boost to public spending. In the seven years to 2006-07, expenditure grew in real terms by 4.6% a year, racing ahead of average GDP growth of 2.7%. The splurge has lifted spending to 42.5% of GDP in 2006-07, nearly two percentage points higher than in the Conservatives' last year in office.

Mr Brown's decision to forsake prudence was doubly unwise. The extra money preceded reforms so that too much of it simply inflated public-sector costs. The health service received the biggest boost of all but much of it has been absorbed by over-generous pay awards that have tipped many hospitals into deficit. The surge in spending was also ill-timed since it coincided with a stretch of weak revenues. For five years running, the chancellor's budgets were too optimistic about tax receipts. The big surpluses melted away like summer snow and the government started

borrowing again. The budget deficit has averaged around 3% of GDP since 2003-04.

Since the general election in 2005, Mr Brown has been trying to make amends. Modest tax increases in two pre-budget reports and the 2006 budget will add up to a chunky £6 billion ($11.7 billion), worth 0.4% of GDP, in 2007-08. The tax burden is increasing a lot more, from 38.1% of GDP in 2004-05 to 40.2% in 2007-08, the highest for almost 20 years. The chancellor is being helped by sharply rising corporation-tax receipts and higher income-tax revenues thanks to “fiscal drag” as earnings rise faster than tax thresholds tied to prices.

Mr Brown is also planning to squeeze public spending from April 2008. In the three years to 2010-11, total outlays will rise in real terms by just 2.0% a year, less than average GDP growth of 2.5%. This will gently ease expenditure down from 42.5% of GDP to 41.9% by 2010-11. By then the retrenchment—compared with keeping public spending at 42.5% of GDP—will cut annual expenditure by £7 billion in today's money, reckons the IFS.

The budget is tightening less than in the late 1990s. But it is still likely to pinch after so long a stretch when the public services have been over-indulged. In a few months Mr Brown, or his successor at the Treasury, will set out how total spending is to be divvied out among individual government departments for the three years starting in April 2008. As the IFS spells out, the chancellor will find it hard to square his commitments to education and reducing child poverty with the demands of the insatiable health service.

But Mr Brown's larger difficulty is that he has failed to make the most of a long stint as chancellor in which he has been blessed with generally favourable economic conditions. For a politician with a reputation for thinking far ahead, his conduct of policy has made little strategic sense. Sharp tightening followed by excessive expansion is a bad way to run things. The chancellor's undesirable legacy will be a bigger state that is palpably failing to deliver value for money for its hard-pressed taxpayers.

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Home Office woes

Prisoner's dilemma

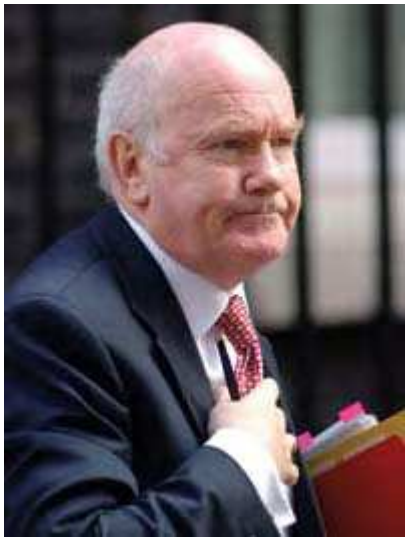
Feb 1st 2007
From The Economist print edition

Problems in the department run deeper than mere bungling

“NOT fit for purpose” is a phrase that John Reid, Britain's home secretary, must be heartily sick of. Nine months ago, when he took command at the Home Office amid a scandal over the release of foreign prisoners, he used it to deliver a kick up the backside to his botch-prone new department. Events suggest that the description still applies.

The bad news lapping at Mr Reid's feet of late bears an ominous resemblance to that which sank his predecessor, Charles Clarke. First it emerged that civil servants had failed to update one of their many databases with details of serious crimes committed by some 540 Britons overseas, leaving them free to apply for jobs from which they might otherwise have been barred. Next the passport service admitted it had let 147 drug traffickers slip through its fingers and defy travel bans. Helpfully, a Sunday newspaper then revealed that 322 registered sex offenders had gone missing because no one had thought to check whether their addresses were accurate. This is disastrous for a government whose professional competence is already doubted by voters (see chart below).

Camera Press



Reid feels the strain

More trouble came when Mr Reid reminded judges last week to hand down non-custodial sentences whenever possible. Two judges have mischievously claimed that Mr Reid's advice caused them to go easy on sex offenders. To top it all, the chief prisons inspector gave warning on January 30th of a crisis in the system: even those who are locked up are not being properly rehabilitated, she said.

Why is the home secretary's in-tray always so hellish? Partly it is because the shifty types his department often deals with do awkward things like giving false addresses. And every mistake is newsworthy: escaped prisoners make better headlines than disgruntled farmers kept waiting for payments due them, for example.

Yet even bearing in mind its difficult remit, the Home Office is poorly run. Last year's civil-service capability review ranked it the worst of the seven departments surveyed, awarding it especially bad marks for “delivery” (ie, getting things done). In two areas it attracted “serious concern”, a label that was not applied to any aspect of any other department.

Last July the Home Office published a short report on how it would put its house in order. Some of its proposals, including a new “contract” to clarify the division of responsibility between ministers and officials, are “bang on the money”, according to Guy Lodge of IPPR, a think-tank. Such reforms are thought to be popular with Gordon Brown, the chancellor and probable next prime minister.

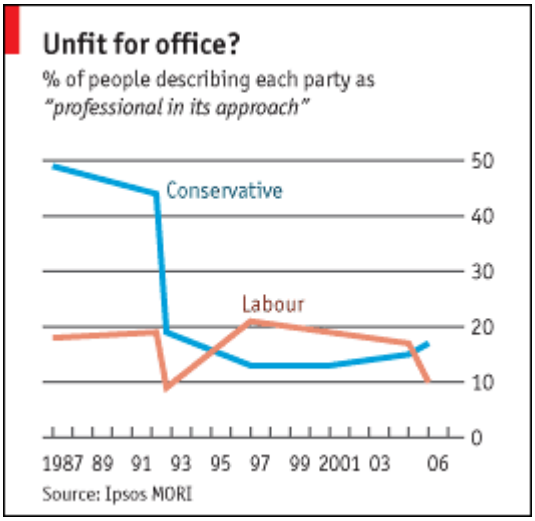
This is encouraging—if the reforms are carried out. Yet it would be misleading to pin everything on delivery, however poor it may be. Many Home Office problems, including overcrowded prisons, are caused by failures of policy, which cannot be solved by reorganising the civil service.

Egged on by the press and desperate not to appear soft, the government's “tough” approach to law and order has helped to swell the prison population from 60,000 in 1997 to 80,000 today. Britain locks up more people per capita than any country in western Europe except Luxembourg (although it still trails behind America).

A crackdown on serious criminals has crowded jails with petty thieves, as tougher sentences for one lot of offenders dragged up the punishments for others. In 1993 there were around 29 shoplifters in prison at any one time; ten years later there were 1,500. Paradoxically, banging up more criminals leads to more crime, as overcrowding makes

rehabilitation programmes less effective. In the past 15 years, as jails have filled up, re-offending rates have increased from 50% to 70%.

It was only sensible of Mr Reid to remind judges that alternative sentences such as community punishment exist; it is just a shame he waited until the last cell was full before doing so. This week he insisted that he had the “endurance” to put things right in his department. Mr Brown may not prove as patient.



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Bagehot

A rough patch for the special relationship

Feb 1st 2007
From The Economist print edition

Steve OBrien

How should Britain deal with a president who appears to have lost all authority at home?

THERE'S nothing new about a little turbulence in the so-called special relationship between Britain and America. Churchill had to put up with Roosevelt's hostility to the British empire. Eisenhower's fury over Suez dealt a lasting blow to Britain's capacity for autonomous action. Johnson was greatly hurt by Wilson's refusal to send as much as a Guards band to Vietnam. Margaret Thatcher was incensed when her soulmate, Ronald Reagan, invaded Grenada, a Commonwealth country, without first telling her. But few periods in this closest of strategic partnerships have been as strange and troubled as the present one.

The source of the problems is the fallout from the Iraq catastrophe. Thanks to it, there is partial regime change in both Britain and America. Without Iraq, Tony Blair would never have felt forced to put a time limit on his premiership—a decision that has undermined his authority and left him a stricken figure during his last months in Downing Street.

For Mr Blair, at least, the end is in sight. For George Bush, humiliated by the Democrats' triumph in the mid-term elections and deserted by leading Republicans, there is the prospect of nearly two years in a political twilight zone. This presents real problems for America's coalition partner and most loyal ally. Working with a brash, over-confident Mr Bush created one set of difficulties for Britain. Dealing with the most discredited president abroad since Richard Nixon (who even at his lowest ebb still had Henry Kissinger) creates an entirely new set.

Some of those difficulties have surfaced since the Iraq Study Group (ISG) reported late last year. The British hoped that a beleaguered Mr Bush would seize on its main conclusions. The emphasis on reviving the Middle East peace process while wooing potential regional allies such as Syria echoed Mr Blair's oft-stated view that “the road to Baghdad runs through Jerusalem”.

There was thus disappointment three weeks ago when Mr Bush swatted aside the ISG's work with a single dismissive sentence that there was no “magic formula” for success. There were doubts in London too about the wisdom of the military “surge” that Mr Bush announced. Though the British government expressed the public hope that the policy might do some good, its private view was that the surge was probably too little, certainly too late, but above all without support in Congress.

Another reason for the lack of enthusiasm was concern that the 7,000 British troops in Basra would be vulnerable if the surge produced a flight of Shia militias to the south of the country. The government is determined to press ahead with plans to cut the size of the force to 4,000 by the middle of the year.

Nowadays there is not much effort to hide these differences. The line ministers initially took—that Britain neither agreed nor disagreed with Mr Bush's new policy—reflected a growing feeling that because Mr Bush is so widely criticised at home he no longer merits exaggerated respect in Britain. One admittedly self-promoting cabinet

minister, Peter Hain, was sufficiently emboldened to talk about how awful it had been for the government trying to maintain a working relationship with what was “the most right-wing American administration, if not ever, then in living memory”.

In a rare debate on Iraq last week in the Commons, which Mr Blair shamefully refused to attend, William Hague, the pro-war Conservative shadow foreign secretary, spoke for nearly everyone in the house when he said it was “a lesson to us all for the future that embarking on military action alongside another power requires confidence...that our allies have a satisfactory plan”. Mr Hague went on to say that there were also lessons to be learned “about the management of our relationship with the United States” and that the case for a high-level Privy Council inquiry into the conduct of the war in Iraq was “overwhelming”. Anti-Bush sentiment in Britain is probably stronger among the war's supporters, who feel badly let down, than among its opponents, who bask in vindication.

Gordon Brown will be tempted to put as much distance as possible between himself and Mr Bush. He may even hold the inquiry called for by Mr Hague. Instinctively more tribal than Mr Blair and with many friends in the upper reaches of the Democratic Party, Mr Brown and the people around him will also find it hard to conceal their longing for a Democrat to win in 2008. As Mr Hain put it: “Our sister party is the Democratic Party, so for me the results in November were fantastic.”

The return of the candid friend

Mr Brown will be making a serious mistake, however, if he allows such partisanship to show or if he thinks he can simply wait until someone more agreeable occupies the White House. John Major paid a high price for rumours that he had authorised Conservatives to dig up dirt on Bill Clinton's no-doubt-boisterous student days at Oxford. There is also serious work that can be done with even this crippled president.

Thanks in part to Mr Blair's constant nagging (or so he would claim), there is a chance that Mr Bush will now go along with establishing a post-Kyoto framework for carbon caps and trading. Similarly, Mr Blair believes that he has helped persuade Mr Bush to put his back into one last heave for a deal on the Doha round of world-trade negotiations. Nor is it inconceivable that, stymied at home, Mr Bush will cast aside his previous objections to active diplomacy in the Middle East and push for a settlement of the Palestinian problem.

In the past, Britain's most valuable contribution to the special relationship has been as the trusted partner who says “yes, but”. Whether Mr Blair was too eager to please or Mr Bush too arrogant to listen, all this president ever heard was “yes”. Mr Brown's job will be to restore Britain's historic role as the candid friend. A humbled Mr Bush might even welcome that.

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Nuclear trafficking

A radioactive subject

Feb 1st 2007
From The Economist print edition

Alex Williamson

Clamping down on the trade in illicit nuclear materials sometimes offends Russia

A CHANCE, you might think, for Russia to show the co-operation that its president, Vladimir Putin, regularly promises in clamping down on the global traffic in dangerous nuclear materials. Yet the release last week of new titbits about a Georgian sting operation which reportedly netted just short of 80 grams of highly-enriched weapons-useable uranium, a Russian citizen from Vladikavkaz in North Ossetia (a part of Russia) and several Georgian accomplices—was a “provocation”, thundered Russia's foreign minister.

The sting was first reported in February last year, and Russia loathes Georgia. But there is more to the Kremlin's nuclear frostiness. While it continues to co-operate with America in securing dangerous nuclear materials around the world—most recently airlifting back to Russia a whopping 286 kilos of highly-enriched uranium fuel from a research reactor in Dresden in former East Germany—Russian officialdom's souring mood at home augurs ill.

Russia is not the only country with a nuclear-smuggling habit. Excluding the Georgian sting operation, a database maintained by the International Atomic Energy Agency (IAEA), the United Nations nuclear guardian, has clocked 16 confirmed cases worldwide since 1993 where highly-enriched uranium or plutonium (both, in the right form, can be used as the fissile core of a nuclear weapon) has been lost, stolen or seized from would-be traffickers, mostly in Europe and Russia. But not all countries bother to report: China, India and Pakistan have been among the 95 contributors to the list only since last year. Coverage is most patchy in the least secure parts of the world, including Africa and the Middle East.

The Georgian case is alarming. The uranium being hawked was enriched to about 90%, and intended for weapons use (fuel for nuclear-power reactors is typically enriched to 5% or less; most research reactors run on more highly-enriched stuff, meaning 20% or more). Georgian officials say their prisoner revealed that his bagful came from an as yet undiscovered stash of 2-3kg; not enough for a weapon—that takes up to 25kg—but still a threat.

This case uncannily resembles one in 2003, when 170 grams of similar material was seized on the Georgian-Armenian border; its Armenian smuggler said he had picked it up in Vladikavkaz too, though tests showed the material had originated at a Russian nuclear site in Novosibirsk.

Though the quantities of weapons-grade material seized by police are usually quite small, the consequences of any falling into terrorist hands are huge. Al-Qaeda's leader, Osama bin Laden, has called the acquisition of weapons of mass destruction a “religious duty”. Some experts think building a bomb is beyond the capabilities of such a group; others don't. But a “dirty bomb”, made by packing conventional explosives around the nuclear waste and other radioactive materials that make up most of the lost or stolen material reported to the IAEA, would be horribly disruptive.

And reported cases may hardly be the half of it. Those trying to find a buyer are more likely to get caught; those who already have one can avoid police stings.

Nor is al-Qaeda the only potential customer. Chechen rebels who attacked a Moscow theatre in 2002 had first considered an assault on a nuclear research reactor at the nearby Kurchatov Institute. Among other terrorist mischief in Russia, an article in the September 2006 issue of the *Annals of the American Academy* lists the casing of nuclear reactors, monitoring the trains that transport Russia's nuclear weapons and even a plan to hijack a nuclear submarine.

At a summit in Bratislava in 2005, the Russian and American presidents agreed to speed a global effort to secure all dangerous nuclear materials. This included repatriating fresh and spent fuel from the more than 100 nuclear research reactors in 40 countries that Russia and America between them supplied during the cold war. Some of these are being converted to run on less dangerous low-enriched uranium. Meanwhile, America's National Nuclear Security Administration is beefing up reactor security in those ill-governed places where it consists of poorly paid guards and flimsy locks.

Russia's concerns about terrorism are one incentive to fix its nuclear problems. Another is huge dollops of American cash. Since the Soviet Union collapsed, America has helped dismantle thousands of surplus nuclear warheads, consolidate a vast archipelago of nuclear materials, and find jobs for otherwise unemployed Russian weapons scientists.

The window for such co-operation is closing, says Laura Holgate of the Nuclear Threat Initiative, an independent outfit that has paid for the return of some Russian reactor fuel from abroad. Much of the easier work in Russia has been done. But officials there still reject help at their most sensitive nuclear sites, where the bulk of the most dangerous materials are kept. Without America looking over its shoulder, says Ms Holgate, it is unclear that Russia will be so conscientious in maintaining security and prosecuting wrongdoers. And if, as Georgia found, it resents being told its nuclear controls aren't perfect, there won't be much outsiders can do to help anyway.

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International law

Controlled explosion

Feb 1st 2007
From The Economist print edition

A new legal front opens against terrorism

SUICIDE-bombings and other systematic violence against Israeli civilians amount to genocide, an American federal judge ruled this week. That is not just politically controversial: it also allows victims to sue the bombers' outside sponsors—in America.

Nina Gershon, a federal district judge in New York, this week cleared the way for plaintiffs to sue the Jordan-based Arab Bank, for allegedly backing terrorism. Ron Motely, their counsel, said that the “precedent-setting” ruling would mean that anyone who aided and abetted crimes against humanity could no longer evade American justice.

Under the Alien Tort Claims Act of 1789, foreigners may sue each other in American courts even for acts committed outside America. These lawsuits rarely succeed. Even when they do, the defendant seldom pays up. But the Arab Bank has a branch in New York.

In 2004 America's Supreme Court recommended that, where possible, such claims should be pressed where the acts occurred or the victims lived. Judge Gershon seems to have decided to ignore this advice in the light of “the universal condemnation of organised and systematic suicide-bombings and other murderous acts intended to intimidate or coerce a civilian population.”

More than 4,500 victims and families, from 12 countries including Israel, claim the bank “knowingly” provided financial and other assistance to the bombers' sponsors. The bank denies the charge and says it “abhors terrorism”. Now it must convince a jury.

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Citizenship for sale

Pledge of allegiance

Feb 1st 2007
From The Economist print edition

Buying citizenship is surprisingly easy

WADS of cash, obliging bureaucrats, and an urgent need for fresh travel papers are a connection that in most countries is dealt with by the police. But there is a respectable end to the trade. In most rich countries a hefty investment brings a visa that can eventually turn into a passport: $500,000 typically secures an American “investor visa”. For the British equivalent it is £200,000 ($392,000). But three countries—Austria, and the Caribbean island states of St Kitts and Dominica—have refined the process further, offering citizenship, in effect, for cash.

My country 'tis of thee

Citizenship application requirements
Average amounts, $

	Austria	St Kitts	Dominica
Investment*	>2.5m	>200,000	None
Government fees	5,000	35,000	82,700
Professional fees	300,000	15,000	15,000
Processing time	9-12 months	3-14 months	5-12 months
Interview	No	No	Yes
Language requirement	No	No	Yes (English)

Source: Henley & Partners *Estimated

For the typical respectable applicant, a rich person from a poor country who wants to avoid hassles with visas, it looks tempting. Awarded to foreigners who provide scientific, artistic, cultural or economic benefits (ie, investment), an Austrian passport—which requires neither prior residence in Austria, nor any knowledge of German—allows visa-free entry to 125 countries and territories; St Kitts and Dominica allow entry to more than 50, including Britain (but not America). Compare that to 25 mostly poor countries for Indian passports. Customers may also be people from countries such as America, whose citizenship may expose them either to terrorism, or to the tax authorities.

Austrian officials say their scheme is rarely used (though statistics are secret) and strictly policed. Applicants have to prove they are making an extraordinary contribution to Austrian life and cases are carefully assessed, says an official at the Ministry of Economic Affairs: “It's not just a matter of handing money over and getting citizenship. It's a really tough process.” St Kitts also emphasises the cleanliness of its 24-year-old system, which has accepted fewer than 500 applicants in total. “There have never been any abuses,” says Shawna Lake of the island's government.

But the right advice can oil the wheels even in the most squeaky-clean system. Henley & Partners, a consultancy, offers to “liaise with the various government agencies and ministries, and then prepare and lodge your application”. Informal approvals from the agencies and ministers concerned, it advises, should be gained before the investment is made.

Few would want to impugn the integrity of Austrian officialdom, which issues, Christian Kälin, a lawyer at Henley & Partners, estimates, only a few dozen such passports each year. Caution is particularly advisable given the way that the passport business has gone awry in other countries. Grenada and Belize sold citizenship widely and unwisely in past decades. In Ireland, a scheme under which 107 passports were issued proved in some cases to have enriched a disgraced former prime minister, the late Charles Haughey.

When that was exposed, it embarrassed some new Irishmen. Having joined what was once termed the “Rolls-Royce of passport programmes”, they achieved unwished-for prominence in the press. The late Mahmoud Fustok, a Saudi diplomat with ties to that country's royal family, organised Irish passports for 15 of his relatives. In 1985 he paid Haughey 50,000 Irish pounds (about $100,000 today) for an investment, he later told a judicial inquiry, in a horse whose details he couldn't remember. That's one way of putting it.

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Mediation

Knocking heads together

Feb 1st 2007
From The Economist print edition

Why go to court when you can settle cheaply, quickly and fairly elsewhere?

THE Bank of Credit and Commerce International's lawsuit against the Bank of England lasted 13 years and cost some £100m ($196m) in legal fees. The Bank of England's governor disgustedly described it as “the most expensive fishing exercise in history”. The presiding judge, Mr Justice Tomlinson, called it a “farce”.

Had the parties agreed to mediation it would have taken probably a day and cost just a few thousand pounds. According to the London-based Centre for Effective Dispute Resolution (CEDR), one of Europe's biggest mediation bodies, of the 3,000 or so commercial disputes that are subjected to mediation in London every year around 70-80% reach a settlement within one or two days, with a further 10-15% settling a few weeks later.

Litigation used to be the natural way of settling disputes, especially in advanced countries. Then clogged courts and ever-costlier lawsuits made arbitration look better, especially in cross-border commercial disputes. But it often proves no cheaper, fairer or even quicker. In America, from filing a complaint to an arbitration decision takes, on average, 16.7 months. So out-of court alternative dispute resolution (ADR) procedures, such as mediation, are now in vogue. The late Sir Michael Kerr, former president of the London Court of International Arbitration, was a leading convert. “In the same way as I have had my mind changed about litigation in favour of arbitration, my long devotion to arbitration is now being eroded,” he said.

Interest in mediation is rocketing, in countries of all legal traditions and none. Karl Mackie, the head of CEDR, talks of a “global revolution”. His outfit, a non-profit organisation that has joined forces with counterparts in the Netherlands, France, Italy and America, is dealing with requests for advice from would-be mediation providers in Saudi Arabia, Russia, Thailand, Japan, Bangladesh, Cameroon, Uganda, Bosnia and Slovenia. As well as in Europe, it is training mediators in countries such as Nigeria, Finland and China, where they can charge up to $20,000 a day.

Whereas arbitration mimics a courtroom setting, with lawyers on both sides and a neutral decision-maker, mediation encourages the parties to talk to each other and strike a deal. The mediator's job is to prompt discussion, not judge the outcome. That is almost always a swifter, cheaper and more flexible way of solving disputes; it is also, if there is any suspicion of judicial corruption, safer. The parties are in control of the proceedings; no solution is imposed; they decide whether to settle.

Set up nearly three decades ago, JAMS, America's main mediation and arbitration service, has more than 200 full-time “neutrals”, as they are known, on its books: mostly former judges, attorneys, or law professors. It handles a fast-rising 10,000 cases a year worldwide. Conventional litigation is suffering: a paper written in 2003 for the American Bar Association by Marc Galanter, a law professor at the University of Wisconsin, coined the phrase “the vanishing trial”. Whereas 11% of civil cases went to court in 1962, that has now fallen to under 2%. The number of federal court tort cases that ended in a trial dropped by nearly four-fifths between 1985 and 2003.

American states including Oregon, California, Texas and Florida have started making mediation mandatory, at least for some claims. Only if it fails may the parties go to trial. Some 1,500 law firms, and 800 companies including Time Warner, UPS, General Electric, the Prudential and Coca-Cola, have pledged to explore ADR in any dispute with another similarly pledged company before litigating.

In Europe, Finland and Denmark are considering similar moves. The European Commission is expected to issue a directive on harmonising mediation this autumn. A UK-China business mediation centre was recently opened with offices in Beijing and London. English courts are increasingly steering parties toward mediation and penalising them (in the award of litigation costs) when they refuse, though the government and the mediation profession are resisting any suggestion to make mediation mandatory. That, they feel, would dilute the whole idea of voluntary participation. But many countries, including Argentina, Australia, Canada, France, Greece, Israel and Singapore, officially encourage the early use of mediation.

The catch, if there is one, is that mediation is confidential. For all their cost, court cases can bring a public benefit by setting precedents, constantly refining and modernising the law. But for those cynical lawyers whose income depends on stoking their clients' outraged intransigence, the growth in mediation may prove to be the end of a lucrative era.

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Correction: James Traficant

Feb 1st 2007
From The Economist print edition

We wrongly stated ("The politics of beauty", January 20th) that the former American congressman James Traficant is serving a prison sentence in Rochester, NY. He is in fact at a federal mental health centre in Rochester, Minnesota. Sorry.

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Britannia redux

Feb 1st 2007
From The Economist print edition

The Bridgeman Art Library

The birthplace of globalisation in the 19th century is coping well with the latest round, writes Merril Stevenson. But can it keep it up?

> To thee belongs the rural reign;
> Thy cities shall with commerce shine:
> All thine shall be the subject main,
> And every shore it circles thine.

“Rule Britannia”, Britain's unofficial national anthem dating from 1740, celebrated not only Britain's military might but its commercial prowess as well. A century later Britain had fully risen to the advance praise. This was the high-water mark of its influence in the world, which coincided with the last great wave of globalisation. The first country to industrialise, Britain was soon turning out more than half the world's coal, pig-iron and cotton textiles. In 1880 its exports of manufactured goods accounted for 40% of the global total, and by 1890 it owned more shipping tonnage than the rest of the world put together.

Less than a century on from those glory days Britain had become the “sick man of Europe”, infamous for wild swings in inflation and growth and for confrontational trade unions. Shorn of its empire and a late and reluctant arrival in the European Community, Britain was grappling with the prospect of irreversible decline.

Now its fortunes are looking up again. Steady economic expansion for the past 14 years has pushed its GDP per head above that of France and Germany. Its jobless figures are the second-lowest in the European Union. Inflation has been modest, and sterling, the Achilles heel of governments from Clement Attlee's to John Major's, is if anything too strong for Britain's good.

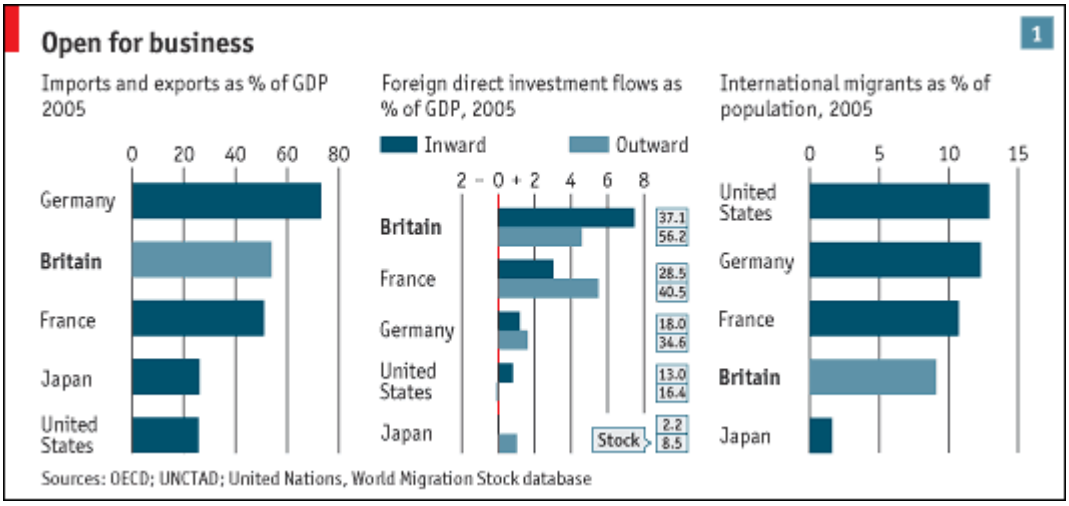
Much of this transformation is due to a quarter-century of profound policy change at home. The Conservatives in government tamed the unions, freed financial markets and unloaded a host of state-owned enterprises. A wrenching decade resulted in a more flexible and competitive economy, though also a more unequal and less cohesive society. A Labour government under Tony Blair sensibly built on its predecessors' work but tried to combine free markets with social justice.

Yet globalisation too has played a big part in defining the Britain that is emerging now. Barriers to the free flow of goods and services, labour and capital are being pulled down around the world, aided by huge improvements in communications and transport. Most countries are embracing market capitalism, including titans in the developing world. It is not just their tennis shoes and computers that are conquering the globe but, increasingly, their software and services, and indeed their capital. Most important, perhaps, they have vast pools of relatively cheap and increasingly skilled workers who put pressure on jobs and wages in rich countries.

Allied with technology, globalisation increases competition and exposes inefficiency. It tends to lessen inequality among countries and increase it within them. In short, though the overall effect is positive, there are losers as well as winners.

Britain's response to all this is worth especial study. As a relatively small trading nation without much in the way of natural resources, it must compete and innovate to make a living. It retains a post-imperial habit of thinking and investing globally, and it is home to the world's most important international financial centre. All this makes it a testing ground for globalisation.

Britain's economy is one of the most open among the big rich countries (see chart 1). Britons have long been avid investors overseas, and now foreign investors are returning the favour: last year Britain was second only to America as a destination for foreign direct investment.



Britain is a little ahead on restructuring its economy too. Its dire economic performance in the 1970s forced an early cure: from the 1980s it de-industrialised with a vengeance, freeing the labour market and strengthening competition. Today Britain does little of the mass manufacturing that countries such as Italy are struggling to defend against lower-cost competitors, and its workforce is much more flexible than France's or Germany's. Much of what is left of its industry is in high-tech or research-based fields such as aerospace engines and pharmaceuticals, where its world-class firms are more than holding their own. Companies were early into outsourcing and offshoring, too. Most importantly, Britain's deregulated financial markets and business services are doing a roaring trade as other countries become more internationally minded.

So the question is not whether Britain is successfully riding the current wave of globalisation: the answer to that is yes. It is whether it can keep coming up with the new products and services it needs to sell to pay for the food and the shoes it no longer produces. And here a few doubts set in.

The first is that Britain is raising its taxes just when other countries are cutting theirs, and is introducing more red tape. But these things have happened only recently and could easily be reversed.

Exchange rates
British pound, January 22nd 2007

	$	€	¥
£1=	1.98	1.53	240

What will be harder to put right is another deficiency regularly flagged up by the OECD: education and skills. Other countries are rapidly moving up the value-added ladder in manufacturing. And thanks to the internet, many more sophisticated services too can now be offered from afar, including legal advice, medical diagnosis, consulting and accounting—just what Britain's educated professional middle class is selling around the world. Universities in India, China and elsewhere are pouring out graduates increasingly capable of doing them. Yet in Britain, for all the talk of the "knowledge-based economy", secondary schooling and vocational training are in a state of permanent upheaval and universities are underfunded.

That is a particular pity, because a more coherent educational system might help to deal with another problem too: a growing social malaise and lack of cohesion. Globalisation is undermining the old certainties in lots of ways: employment is less secure, communities less rooted, the gaps between rich and poor, skilled and unskilled, young and old, are wider, and immigration has risen sharply in recent years. All this has created vibrancy and buzz, but also dislocation and often a sense of grievance. The discovery of substantial pools of home-grown Islamic terrorists has added a frisson of fear.

Britain is in some ways a halfway house between America and the rest of Europe. It more closely resembles its transatlantic cousin in its open and flexible markets, but it shares its commitment to social safety nets with other EU members. At every turn the choice lies between openness and protectionism, between multiculturalism and nativism, between engagement and isolationism. Which way will it go?

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A lost opportunity

Feb 1st 2007
From The Economist print edition

A golden decade has transformed the economy less than it should have done

"IN 1997 the challenges we faced were essentially British," Tony Blair told the Labour Party conference last September. "Today they are essentially global...The question is not about our competitiveness in the last ten years but in the next ten."

To be fair, Gordon Brown, the chancellor and Mr Blair's likely successor as prime minister, has had his eye on global competitiveness all along, as a heap of initiatives attest. Macroeconomic stability, coupled with microeconomic measures such as tax incentives and a stronger competition regime, was to sort out the familiar British complaints of low productivity, low business investment in research and development (R&D) and fitful innovation. He largely achieved his macroeconomic goals and did well enough with his microeconomic policies, as far as they went.

Mr Brown was lucky to inherit an economy in which much of the heavy lifting had already been done. The financial markets were flourishing. Margaret Thatcher's union-bashing in the 1980s had resulted in a more flexible labour market. Foreigners had responded to Britain's improved prospects by investing piles of money, which often lifted standards of management and productivity (as Japan's Nissan and Honda did in carmaking). And though the Conservatives failed to avoid two recessions and a humiliating eviction from Europe's exchange-rate mechanism in 1992, they learned from their mistakes. When Labour came to power, it took over a growing economy with a current account that was moving towards balance, a budget heading towards surplus, and a Treasury that had been using an explicit inflation target to steer monetary policy for five years.

Mr Brown built on that success. His boldest move was to give the Bank of England freedom to set interest rates to meet the government's consumer-price inflation target, currently set at 2%. He also managed to keep Britain out of the euro.

Average annual economic growth since 1997, at 2.8%, has been above its post-war trend rate of 2.5%, despite slowdowns in 2002 and 2005. Some 2.5m extra jobs have been created, pushing the proportion of the workforce in employment to its highest level since the 1970s (though the number of jobseekers has also increased with immigration and higher participation among older workers). Under the Bank of England's guidance, price increases were kept close to the Treasury's target, at least until dearer fuel helped to push consumer-price inflation to 3% in December. Confidence that inflation would be contained also muted pay rises. In his pre-budget report in December, Mr Brown forecast that growth in the coming fiscal year would be around 3% and that inflation would move back towards the target.

Temporarily supercharged

But the economy has been helped by three special factors that cannot be expected to continue indefinitely. The first is that the government has been spending well above the rate of economic growth since the end of its first term in office. Spending on education, transport and the National Health Service doubled. At first that did not seem unreasonable, because the economy had been weakened by the collapse of the dotcom boom. But revenues repeatedly fell short of forecasts, so the public sector swung into a big deficit in the fiscal year to March 2002 and has stayed there ever since. Moreover, some big liabilities, such as private-finance initiatives to build schools and hospitals and prisons, are not fully reflected in the accounts. The same is true for public-sector pensions.

The second boost to growth has been a debt-propelled consumer boom sustained by house prices that have almost trebled in a decade. Household debt has leapt from around 100% of disposable income in 1997 to 160% in 2006. Interest rates have been raised three times in six months. At some point the consumer is bound to stumble.

The third factor has been an enormous influx of immigrant workers—around 600,000 from new members of the European Union alone since May 2004 (though some will have left again). The National Institute of Economic and Social Research, a think-tank, estimates that new immigrants have boosted output by more than 1% since 2004 (and by over 3% since 1997). But as other EU countries open their labour markets, the flow to Britain may dwindle.

Yet despite more than a decade of unprecedented stable growth, two problems in particular remain unresolved. One is productivity, about which more below. The other is the persistent deficit in the current account of the balance of payments.

Like most advanced economies, Britain has seen its share of world exports decrease as that of industrialising countries with lower costs has risen. It successfully sells high-value-added products such as pharmaceuticals, telecommunications and aerospace engines, but sterling's strength has not helped. The deficit worsened as Britain grew faster than its main trading partners in Europe. Exports began to pick up last year along with growth in Europe, but the deficit in goods topped £82 billion in the year to September 2006.

The surplus on services filled more than a third of that hole, and net investment income from abroad about another third. The question is whether this bonanza can continue. Britain's liabilities abroad officially exceed its assets, to the tune of 18% of GDP in the 12 months to September, and the gap was bigger than the year before. Are British investors just better at wringing a return from their money?

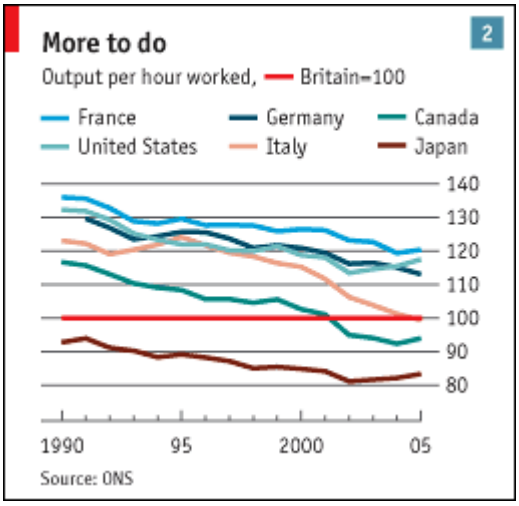
Stephen Nickell, until last year one of the economists on the Bank of England's Monetary Policy Committee, puts forward a couple of explanations. One is that the British tend to go for equity-type investment whereas foreigners go for debt. Equity investment is riskier, so returns tend to be higher. Second, much of British investment abroad is direct—ie, buying companies, starting new ones, reinvesting the profits—and that is harder to value than portfolio investment. He thinks that if official figures reflected the market value of direct investments, Britain's assets would be worth a lot more than its liabilities.

Reasons not to be complacent

The dangers are that returns on equity may not always exceed returns on debt as handsomely as they do now; that the continuing appreciation of sterling will diminish the value of British assets abroad and increase that of its liabilities; and that as Britain itself attracts more foreign direct investment, its traditional surplus on that score may be eroded. Foreigners are buying British firms in droves. The cheekiest offer has come from NASDAQ, an electronic exchange in America, for the heart of the City, the London Stock Exchange.

Productivity, the biggest single component of competitiveness, is a second area where progress has been disappointing. Historically labour productivity has been low in Britain: on average, its workers turn out less per hour than their opposite numbers in France, America or Germany (see chart 2). Though the gap has narrowed in recent years, the differences remain large.

This is puzzling, because Britain's steadily growing economy, stable prices and competitive markets ought to have brought substantial gains in the past decade. The most important reason may be poor skills. Yet it is not the only one: the British workers who make cars at Honda's plant in Swindon are as productive as their opposite numbers in other countries.



Another factor is the increasing weight of the state. The current Labour government has added around 700,000 public-sector jobs to the economy—just over a quarter of all the new jobs created. Productivity in the public sector is hard to measure and often poor.

Fairly full employment may also play a role. If almost everyone is working, less skilled and motivated people also get jobs, reducing overall productivity. That might explain some of the differential with France and Germany but not with America, which also has high employment.

Another explanation is that productivity is usually higher in businesses where employees work with machines or technology. The service sector, which is less capital-intensive, employs a bigger share of the workforce in Britain than it does in Germany, for instance—but again that does not explain the gap with America.

However, two other things might. First, America has made particularly big productivity strides in retailing, where big firms such as Wal-Mart have been able to open sprawling warehouses and superstores around the country. Britain's shopkeepers do not have the luxury of space and looser planning rules to put a handful of workers in charge of acres of goods, so retail productivity gains have been much lower. Second, British companies operate with lower capital stocks than many of their competitors, and their lorries have to drive on heavily congested roads. They often invest respectable sums in computers and information technology but do not seem to reap the same productivity gains from it as many American firms, according to John van Reenen and Nick Bloom of the Centre for Economic Performance at the London School of Economics.

In a study with John Dowdy of McKinsey, a consultancy, Mr van Reenen concluded that British managers are partly at fault. Britain has a lot of family-owned and family-run businesses, more than Germany (where family-owned businesses are usually professionally managed) and many more than America. Britain's multinational companies have good productivity levels, and the best domestic firms are not far off, but smaller ones often struggle.

Perhaps because of blinkered bosses, Britain has a history of underinvestment by both business and government, especially in research and development. Again, that may reflect the sort of businesses that dominate the economy rather than a lack of spending by specific firms (GlaxoSmithKline, for example, is the world's third-biggest pharmaceutical investor in R&D). But it does affect overall productivity.

At the same time heavier taxes and more regulation are beginning to weigh on firms. In the past ten years the tax burden has risen from 34.8% to 37.3% of GDP, higher than in America, Japan or even Germany. And the British Chambers of Commerce estimate the direct cost to businesses of complying with rules brought in since 1998 at more than £50 billion.

Britain is never far from the top in various league tables that measure competitiveness, but it has recently slipped a bit. The World Economic Forum in Switzerland demoted Britain from ninth to tenth last year, citing the burden of government compliance among other weaknesses. Such slight slippage does not constitute a trend. But more red tape and higher taxes, if unchecked, risk clipping the wings of Britain's high-flying firms.

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Living by their wits

Feb 1st 2007
From The Economist print edition

Eyevine

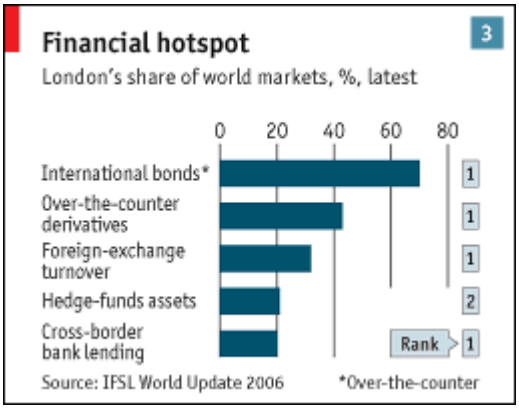
Sharpened by competition

CANARY WHARF rises sleek and shining from the banks of the Thames as the river winds through what were once derelict docklands. This is now the eastern outpost of the City of London, the traditional square mile of banks, brokers and insurers around the Bank of England. Together, the two make up the centre of Britain's financial dealings, and much of the world's besides.

At Barclays Capital's investment-banking floors in South Colonnade, the trading desks are humming. Numbers spool across 5,700 screens as dealers buy and sell swaps, options and much more with counterparts in New York, Hong Kong or Zurich. A low babble is broken by heavily-accented screams of delight or anguish: more than half of Barcap's staff worldwide are foreign. At Birley's sandwich shop downstairs, Antonio, Tomasz and Karim slice salt beef for their customers.

The City of London is globalisation in action. It is, first of all, thoroughly international, handling more of the world's deals in over-the-counter derivatives, global foreign equities, eurobonds and foreign exchange than any other financial centre (see chart 3). Second, its firms specialise in innovative, high-value-added products. Third, the City is living proof that clusters work in the way that economists claim. Capital can move like mercury. The main reason why international finance has made London its home is that everyone is there, making it easier to do complicated deals and to trade quickly in large quantities. The City offers a cluster of talent—financial whizz-kids, lawyers and due-diligence accountants—that is second to none, and self-renewing. It helps that English is a near-universal second language and that London's time zone makes it possible to trade in a (long) working day with both Asia and America. Regulation is mainly deft but not lax, and the taxman takes a hospitable view of foreigners' personal earnings.

Fourth, it turns out that the biggest all-round powerhouses are not British but American, German or Swiss. This has come to be called, with a hint of ruefulness, the “Wimbledon effect”. As in tennis, Britain hosts the tournament where the world's best compete, but it rarely goes home with the cup.



Bowler hats to running shoes

London was not always the hustling, bustling place it is now, though it has long had form in finance. Its first institutions—the Bank of England, the insurance market at Lloyd's—were created three centuries ago. In the 19th century, when Britain dominated world trade, the City was the most important financial centre anywhere. London's fortunes later slipped with those of Britain's economy, though international business picked up again in the 1960s.

What transformed the City two decades ago, however, was the sudden arrival of all-out competition. Big Bang in 1986 blasted open a cosy London Stock Exchange, abolishing restrictive practices and opening the way to a creative free-for-all. Banks and other financial firms poured in, many from America, Germany, Switzerland or Japan, to take advantage of a freedom they did not enjoy at home. After a difficult decade the City blossomed. First, London stole the new euro markets from under the nose of Frankfurt; then America overdid the regulation after the scandals at Enron, so many firms seeking listings chose London instead.

“The government, under Labour and the Conservatives, gives itself too little credit for making financial institutions grow up and have to compete with the best in the world,” says Bob Diamond, the American boss of Barclays Bank's investment-banking and investment-management divisions. The eventual strength and stability of the British economy was helpful to firms like his that were trying to make their mark in this globalised business. So was the willingness of Barclays Bank's top brass to pay the high-flyers at its capital-markets fledgling more than their seniors in the commercial bank.

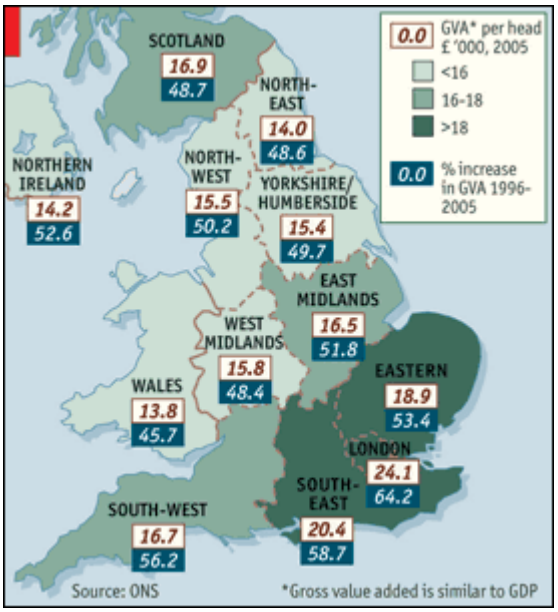
The advent of the euro in 1999 at first seemed a mixed blessing. Sterling did not join the common European currency, so big British banks could have been sidelined had not British corporate clients given them mandates to raise money for them in the new currency. Barclays, for one, has never looked back. It now does more international bond deals than any other firm.

What could challenge London's pre-eminence? Terrorism, for a start. The City proved resilient in the face of the London bombs on the morning of July 7th 2005: full share-trading resumed that same afternoon. But the financial community knows that London is an important target for Islamist terrorists, and worries about it.

There are commercial threats as well. American politicians are preparing to lighten regulation at home to lure companies back to New York. Some business is being switched from London to lower-tax jurisdictions such as Ireland and the Caribbean. Back-office operations are drifting off to places where costs are lower, such as Glasgow or Bangalore. And new competition is on the way. Dubai's international financial centre is likely to grow stronger on oil revenues in the region, and Shanghai, with China's expanding economy behind it, could attract a growing share of international business.

But for now, the City generates a fifth of all corporate-tax revenues in Britain, according to Oxford Economics, a think-tank, and it does so with fewer than 350,000 direct employees. Many of these people get paid a lot. Fat pay packets have helped London house prices to triple over the past decade. London traffic remains sticky, despite the congestion charge. London has become one of the dearest cities in the world, and the young and the middle classes working outside financial services find it ever harder to get a foothold.

The rush of money to London has also increased two other gaps. The first is between rich and poor. Income is distributed more unequally in Britain than in almost any big rich country except America. Over the past decade the move to even greater inequality has been slowed by government policies such as the minimum wage and various benefits for the poor. Even so the pay of the very top earners has rocketed whereas the disposable income of average households has risen only modestly.



The second gap is that between London and the south-east on one hand and the rest of the country on the other. After decades of mine and factory closures the regions are growing, thanks in large part to a surge in central-government spending and employment there. Some cities, such as Manchester, Leeds, Newcastle and Glasgow, are managing to restructure their physical and economic base, regenerate their inner cities and attract business-service firms, and encourage science and technology parks around their universities. But London and the south-east are

growing even faster (see map), drawing in bright young people and contributing to awful housing and transport bottlenecks.

From wonks to widgets

For all the growing dominance of the service sector, Britain still makes and exports things. Manufacturing has grown steadily, if less rapidly than services. For a smallish post-industrial country, Britain has a surprising number of giants. Vodafone is the world's biggest mobile-phone company by revenue; GSK is the second-largest pharmaceutical; Rolls-Royce is one of three makers of aero engines; JCB's earth-moving equipment is made and bought around the globe. Smaller firms too are looking abroad for suppliers and markets. A recent survey of firms of all sorts and sizes by the Institute of Chartered Accountants of England and Wales found that three-quarters of them were involved in international business of some sort.

For Sir Christopher Gent, the chief executive who made Vodafone a world-beater (and who has since become chairman of GSK), the firms that succeed are those that have an international outlook to start with. “It goes back to our history as a trading nation and to the free-trade movement. And we have a very open economy, particularly in my industries, which are technology- and science-based,” he says.

Telecoms had its own Big Bang in 1986, a month after the City did, when the European Commission decided on GSM as the first digital standard. This opened up a mass market on an international scale. Vodafone soon looked outside Britain for partners. Two takeovers gave it a global role. The first, in 1999, was of America's AirTouch, which came with the rights to operate in a number of countries. The second was of Mannesmann, a big German rival. Vodafone's profits have since come down to earth as competitors have turned equally global.

For GSK the international dimension was important too: both Glaxo Wellcome and SmithKlineBeecham were global businesses even before they merged. GSK spends 40% of its £1.3 billion R&D budget in Britain (where it makes only 5% of its sales) and the rest mainly in other European countries and in America. Much new development, however, is going to India, Singapore and China.

Britain's creative industries are no global slouches either. Film and television exports in 2005 were sharply higher than four years earlier. Britain's WPP, an acronym behind which lurk names such as J. Walter Thompson and Ogilvy, is the largest advertising agency in the world. Sir Martin Sorrell, its chief executive, explains why creative firms are doing well: “Many of them were relatively newly formed and didn't have so many legacy issues. People get into senior positions earlier. New technology also had a bigger impact on our business than on some others, so that encouraged change.” WPP's core clients were going global and wanted their advertising agency to do the same. These days only 15% of the firm's business is in Britain—and it is the market leader in Asia.

Britons have bought up foreign firms and expanded abroad for years, where local rules permitted them to. But foreigners are now shopping even more enthusiastically in Britain, because national champions are not protected. Foreign firms own everything from London's water supply to its airports and are about to pocket what remains of Britain's steel industry.

Time was when that would have caused a lot of upset. Richard Lambert, the director-general of the Confederation of British Industry (CBI), recalls that in the 1980s, when Pilkington, a big glassmaker, received a hostile bid, there were marches and protests in St Helens, the firm's home town in north-west England. Then Pilkington itself went global. When a Japanese firm took it over early in 2006, no one raised an eyebrow.

There were whimpers when Rover, the last British-owned mass carmaker, was finally dismantled by Chinese creditors in 2005, but the government paid out only £15m to help the workers, and that was just before an election. Britain, after all, is still exporting 1.3m cars a year under American, French and Japanese labels. Sir Callum McCarthy, head of the Financial Services Authority, says the last time a foreign takeover in the financial sector caused a stir was in 1999, when the Bank of Scotland launched a hostile takeover bid for England's National Westminster Bank.

In a global economy with mobile capital it can be hard to say where ultimate ownership lies anyway. The real test is whether a foreign buyer manages the investment in Britain well and improves productivity. “I don't mind if Spain owns Terminal 5 [at Heathrow airport] because they can't take it back with them,” says Sir Digby Jones, a former boss of the CBI.

Hiring, not firing

“In future we'll live by our wits. We have no real natural resources,” says Ian Barlow, senior London partner of KPMG, an accounting firm. But wits are harder to find than they were. Businessmen give the government credit for good economic management and the promotion of free trade. What many worry about, beside transport, taxes and red tape, is talent. With some 1.2m manufacturing jobs gone in the past ten years, some employers are beginning to feel the culling may have been overdone. Rolls-Royce is having to hire engineers in Germany and elsewhere because

it cannot find people with the right skills at home. Indro Mukerjee, the chief executive of C-MAC MicroTechnology, is worried about the drop in students taking degrees in engineering, “something that has such a great British pedigree”.

Barclays' Mr Diamond, too, says that his company is now hiring heavily overseas, especially in India, and the quality is “absolutely jaw-dropping”. So what is to be done? “Above all, skill the people,” says Sir Digby. “Everyone has to go up a notch.”

When Mr Blair came to power almost ten years ago, he put education at the top of his priority list. If education is still in a mess it is because Labour has done too much, not too little.

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Suck it and see

Feb 1st 2007
From The Economist print edition

The hazards of being an entrepreneur

IN 1978 James Dyson (then an impecunious art student turned inventor, now knighted) ripped the bag off an old Hoover vacuum cleaner, fitted a foot-long cardboard cone instead and flipped the switch. Thus was born the bagless ancestor of what today is the bestselling vacuum cleaner in Britain, America and much of the rest of the world.

But getting there was not simple. Sir James made 5,127 prototypes before the dual-cyclone technology and sleek design was perfected. For three years he lugged the final version around Britain, then the world, looking for someone to make it under licence. In the nick of time a Japanese firm took him seriously. Japanese consumers fell in love with the pink-and-lavender “G-Force” which retailed for £1,200 ($2,000). He was on his way.

Eyevine

Serial inventor

In 1993 Sir James set up his own plant in Britain's rural Wiltshire. By the end of the decade his bagless vacuum cleaners were bestsellers in Britain and doing increasingly well abroad. His factory was churning out 800,000 machines a year.

These days Dysons are no longer made in Wiltshire but in Malaysia. Production was shifted because there were no longer any suppliers near the original factory, the wage bill per person had doubled and the local authority had refused planning permission to expand.

The decision to move abroad caused a storm, yet things have turned out just as globalisation advocates would have hoped. Three factories in Malaysia now make 4m vacuum cleaners a year, with all the suppliers within a ten-mile radius, at one-third of the cost in Britain. The Wiltshire factory has become a research and design centre; Dyson employs more people than before, and in more highly skilled jobs. A new phase of R&D has produced a miniature digital motor with a power-to-weight ratio five times that of a Formula 1 racing car, which is being used in a tiny new vacuum cleaner and a super-hygienic, energy-efficient hand drier.

The company now has a turnover of around £600m, 80% of it from exports. It is spending about £60m on R&D this year, and pays taxes on all earnings to the British government. Last year there was enough left in the kitty for Sir James to pay himself a salary of £31.5m, which is more than any FTSE 100 chief executive gets. He is also setting up a design school in Bath for 14-to-19-year-olds.

Innovative firms like Dyson can grow from small beginnings to world-beaters. Global competition is turning many products into commodities, so innovation is essential if companies—and countries—want to stay in business.

Britain has plenty of people with good ideas and entrepreneurial ambitions: a poll by YouGov last year found that one person in three wanted to run his own business. But in 2005 only just over 6% of British workers started a business or had done so in the previous three and a half years. In America the rate is double that.

The reasons often cited for entrepreneurial reluctance in Britain include fear of failure, lack of finance and a shortage of suitable projects. Poor marketing and management skills and poor infrastructure are also blamed. Yet the problems are clearly not insuperable: witness the blaze of creativity in Britain's financial services.

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Clever stuff

Feb 1st 2007
From The Economist print edition

Education and skills are Britain's weak spots

THE noise in the auditorium at the Lilian Baylis Technology School in south London is excruciating. It is capitalism in full cry. Sixteen students of various hues, all aged around 13, have spent the morning designing and setting up their own virtual businesses. When the whistle blows, they have five minutes to pitch to five independent student buyers. Then another whistle, a session of full and frank criticism ("He charged me £500 for the hotel room and her only £10"), an award for the student who has sold the most and certificates for all. Afterwards, the participants say that they found it really hard to please customers—but over half of them have decided they want to set up their own businesses when they grow up.

Black Ink Photographic

An entrepreneurial spark at Lilian Baylis School

Kennington is a not particularly salubrious part of London. Many of the students at Lilian Baylis come from poor families, a quarter are refugees and most belong to ethnic minorities. This virtual-market exercise was one of a number of events organised for schools by Entrepreneurs in Action, a not-for-profit outfit created to open young people's eyes to possibilities in the business world. In his time its founder, Derek Browne, who did not shine at school, has been an international athlete and an investment banker. "I want to raise these kids' self-esteem," he says, "and show businesses that there is a lot of talent where they don't always look for it." He is part of a broader effort to involve businesses more closely with schools, especially in poor areas.

Lilian Baylis is doing well: in 2005 it ranked in the top 2% of secondary schools in England for "contextual value added", ie, raising students' achievement above the level suggested by their background and previous attainment. But this is hard to do. The problem, says Gary Phillips, the headteacher, is that mainstream academic exams, which many children find hard to engage with, and teaching other skills, including creativity and problem-solving, do not mix easily.

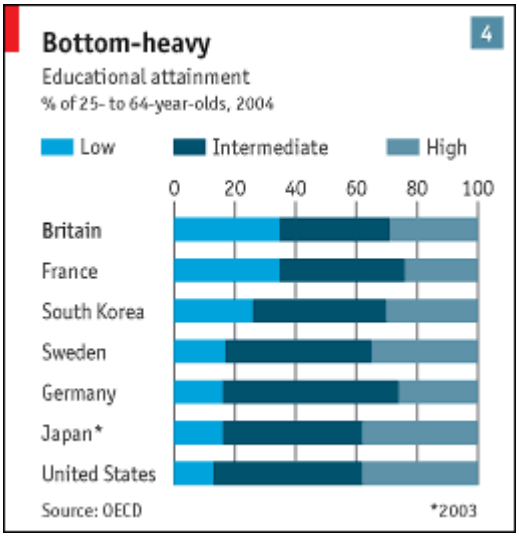
Britain seems as far from resolving that dilemma as it was 62 years ago when universal secondary schooling was introduced. Yet striking the balance between technical and academic education, and making sure that both are worth the paper they are written on, is the biggest challenge facing Britain. It matters every bit as much for social peace and cohesion as it does for economic competitiveness.

At its Etonian or Wykehamist best, British education is superb, but that is not the sort most children are getting. The run-of-the-mill stuff suffers from problems that go back a long time, including poor basic skills, a tendency for students to leave the minute they finish compulsory schooling at 16 and the lack of a coherent and valued system of vocational training. The result, as chart 4 shows, is that Britain has a fairly good stock of graduates but is undersupplied with mid-level skills.

Start with basic literacy and numeracy. More than one-third of British adults have left school with no formal qualifications. About one-sixth are functionally illiterate and one-fifth innumerate, meaning they cannot read and write or deal with numbers as well as an average 11-year-old.

All this is bad enough in itself, but it is especially dire if you are hoping to

compete by producing high-value-added, innovative goods and services. According to the OECD, Britain ranks only 13th among its 30 member countries for the share of people aged 55-64 who have completed secondary school. In younger age groups it is doing even worse: for those aged 25-34 it ranks a worrying 23rd. Although more young people are staying on at school, Britain is being outclassed by countries such as Ireland or South Korea.



The Labour governments of the past decade have been trying hard to improve things. More teachers were hired, and all were told how to teach. Targets were set, a raft of new programmes was launched and lots of computers were put into classrooms. Spending per pupil all but doubled, from £2,000 in 1997 to £4,000 in 2005. Poor students aged 16-19 were given a weekly cash allowance to persuade them to stay on at school. A £40 billion programme to rebuild or refurbish every secondary school in the country over 15 years took off in 2006.

But a passionate ideological debate about selection in English education (Scotland, Wales and Northern Ireland have their own systems) has got in the way. Politicians have been so intent either to defend or to oppose selection by academic ability that they have failed to set up a system of rigorous and useful qualifications for those whose interests are not academic. Standards have suffered in the name of inclusion, and vocational training has been chaotic. Meanwhile the great divide between public and private education has remained as important as ever.

With the targets and the cash eventually came attempts to give schools more autonomy, identity and outside sponsorship. Parents were promised more choice. Some schools, including Lilian Baylis, chose to apply for “specialist” school status. Failing schools in poor areas are being replaced by “academies”, sponsored and part-financed by businesses or charities. Following contentious legislation in 2006, all schools will be encouraged to bid for “trust” status, linking with other schools or businesses to create schools with a distinctive ethos and considerable autonomy from local-education authorities.

At first glance, all this has produced some impressive results. More young people seem to be hitting the targets, taking exams, staying on at school and going on to university. An increase in primary-school skills should eventually improve results all along the line.

But secondary schools remain a problem. The proportion of students obtaining five good grades in the GCSE exams taken at the age of 16 has risen from 45% in 1997 to 57% in 2006. But of those whose GCSE subjects included English, maths, a foreign language and a science, all once core subjects in the curriculum, the proportion gaining good grades has dropped from 30% five years ago to 26% last year. In other words, students appear to have done better because they have been picking easier subjects. Something similar has happened with A-levels, taken at 18, where a quarter of all exams are now thought to be worth an A, against 12% 15 years ago.

GCSE entries for foreign languages have fallen by 37% in five years, according to CILT, the national centre for languages. Much of that drop is due to the removal in 2004 of the requirement to learn a foreign language. Interest in single sciences (physics, chemistry, biology) has also plummeted. The number of students taking physics at A-level, for example, has halved since 1988, according to the Centre for Education and Employment Research at the University of Buckingham. Chemistry, too, is on the slide as students choose broader and less rigorous science courses.

In response to its critics, the government is pursuing reforms in three areas. First, it is overhauling Britain's vocational education. To boost skills and encourage teenagers to stay on at school it is introducing a new system of diplomas, giving 14-19-year-olds the chance to enrol in a work-related course, with a core of basic skills taught alongside. A government report estimates that perhaps 40% of teenagers will abandon GCSEs over the next ten years to study for diplomas instead, offered by secondary schools or nearby colleges of further education. But so far no one seems clear what the courses will entail, and some fear that schools may not have the resources to teach them. Some argue, too, that students should not be shunted off into exclusively vocational training but keep the option to go back into the academic stream.

A second line of attack is to improve the skills of those already in the workforce. In December a commission headed by Lord (Sandy) Leitch proposed spending more money on training and giving employers a bigger say in what the training should be.

The third reform is to give able academic students tougher options. A new, more challenging layer is to be added to A-levels, and more state schools will offer the broader International Baccalaureate.

Awakening spires

Higher education too is in the firing line. It has expanded far faster than the ability of taxpayers to pay for it. Gone

are the days when only the elite aspired to university: some 40% of the age group now go on to higher education. Red brick has given way to concrete slab, polytechnics have been granted university status, and the lines between universities and colleges of further education are blurring.

Britain is home to two of the world's top ten universities, according to the world ranking drawn up by Shanghai's Jiao Tong University. Oxford and Cambridge are the only non-American institutions on the list. To stay there, and to continue to attract, as British universities do, more than 15% of the world's international students in higher education, the sector's finances need reforming.

Higher education has traditionally been free in Britain. As student numbers increased and government support remained much the same, funding per student fell by 36% in real terms between 1989 and 1997. A tuition fee of £1,000 a year (waived for poor students) was introduced in 1998. Five years later, in a move intended to shake up higher education as well as pay for it, the maximum fee was increased to £3,000 from 2006. Students were offered loans and universities told to provide bursaries for poor students.

So far, few universities have chosen to differentiate themselves on the basis of the fees they charge, or to charge different fees for different courses. The £3,000 is not enough to allow for much manoeuvring. Universities also get a continuing government subsidy of £4,000 or so per undergraduate, as well as much higher fees from foreign students, money from research contracts and income from endowments. But these do not cover costs at the top universities: Oxford, for example, reckons that on average it takes more than £12,000 a year to teach an undergraduate.

So universities are racing to find other sources of funds. Alumni who have not heard from their *alma mater* in years are suddenly bombarded with calls. Alison Richard, vice-chancellor of Cambridge University, taught at Yale and had the opportunity to observe the legendary management of that university's endowment. Cambridge has now smartened up its arrangements.

Universities need many sources of finance if they are to remain independent and competitive, including profits from commercial activities. Many have established science parks to attract big research contracts and set up “incubators” to encourage small firms to spin off discoveries into commercial ventures.

The customer is king

As higher education has expanded, it has become increasingly obvious that not all universities, and not all degrees, are equal; and now that students are paying for their education they are beginning to behave more like consumers. At some universities they are demanding more for their money—more hours of tuition, harder assignments. Many also seem likely to choose courses with the largest possible future earnings potential. In the past, a university degree in Britain promised a bigger income premium than in most other OECD countries. Now that its scarcity value has gone, says Anna Vignoles of London University's Institute of Education, initial average returns to degrees are very small. But those who study “hard” subjects such as accountancy, law, medicine, engineering or maths continue to enjoy a premium. That may start a swing back to those subjects.

A similar invisible hand may also work in the market for vocational qualifications. Until now, most of these have attracted little in the way of extra pay, and some have actively put off potential employers: the Institute for Fiscal Studies, a think-tank, calculates that low-level vocational qualifications actually inflict a pay cut of 5-20% on their holders, who are labelled as dummies. As the financial value of some university degrees sinks towards zero, training as a plumber or an engineer will look more attractive. And such jobs cannot easily be transferred abroad.

Britain, unlike Germany, has never had a coherent system of vocational education, despite all the talk about the importance of skills and human capital. Critics say that new paper qualifications have raised young people's hopes, but have not led either to university or to a job. That is particularly true among some of Britain's ethnic minorities.

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A house with many mansions

Feb 1st 2007
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There is nothing wrong with multiculturalism. The problem is terrorism

"EXPORTING services is the easy part of globalisation; importing people is the tricky part," says David Willetts, the Conservatives' education spokesman. Three miles east of the City, the borough of Newham is living proof.

Newham lays claim to being one of the most diverse places in Britain. In the Romford Road that runs across it, the Minhaj-ul-Quran mosque faces an Afro-European hairdresser, with the Radha Krishna temple and a Chinese restaurant nearby. Up the road, JB's Dance Studio advertises salsa classes, and a house in a side street displays a rare St George's flag. According to the most recent census, in 2001, Newham is 39% white, 33% Asian and 22% black, and its residents rub along together pretty well. Trouble, when there is any, tends to come from outside.

Alamy

Side by side

It did last June, when a couple of hundred policemen burst into a modest house in the Forest Gate area one night and hauled off two bearded brothers on suspicion of involvement in terrorism, shooting one in the shoulder. Almost a year earlier, in the wake of the London terrorist bombings in July 2005, the police had shot dead an innocent Brazilian in a south London Underground station, mistaking him for a terrorist. So when the police found nothing at Forest Gate, Britain tensed and several Muslim groups threatened to march in protest. There was a collective sigh of relief when the brothers were later released.

Now Newham is again at the centre of controversy. Plans have been drawn up to build the biggest mosque in Europe on a brownfield site next to what will be the Olympic stadium when London hosts the games in 2012. The new complex is designed to hold 40,000-70,000 worshippers, more than ten times as many as the largest Anglican church in Britain. It would dominate the view of London of millions of visitors to the Olympics.

The mosque-builders have not yet applied for planning permission, and may not get it if they do. Yet the proposal has touched a raw nerve, and not just because of its size. The sect behind it is the secretive Tablighi Jamaat, which claims to be above politics, but three prominent British terrorists are thought to have been members.

Many of Newham's Muslims, as well as its Christians, have reacted with outrage to the proposal, claiming that the mosque would risk radicalising young people and worsening community relations. And as if that were not divisive enough, an enormous evangelical, mainly black, church in the neighbouring borough of Hackney, where some Christians from Newham worship, is being kicked out of the area to make way for Olympic construction.

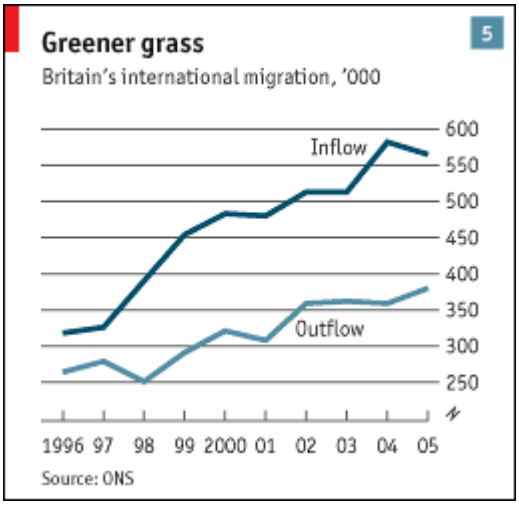
The events in Newham are part of a wider and increasingly anxious debate over race, religion and identity in Britain. That debate goes back some way. In 1966 Roy Jenkins, then the home secretary in a Labour government, argued for a multicultural model of immigration: "Not a flattening process of assimilation but equal opportunity accompanied by cultural diversity in an atmosphere of mutual tolerance." Whereas the French, for example, dealt with diversity by insisting that everyone conform to the same secular rules, Britain allowed, even encouraged, its ethnic minorities to carry on in their faiths, languages and customs. But two recent developments—sharply higher immigration from 1998 and the discovery of home-grown Islamist terrorism in 2005—have raised questions about this approach.

Apply here

In the main, Britain has been a net exporter of human capital. It was not until 1983 that many more people started arriving than leaving. Since the late 1990s, however, the number of immigrants has shot up (see chart 5).

Not only are there many more immigrants than there were but they also come from a larger variety of places. The initial wave had come from Commonwealth countries in the Caribbean and the Indian subcontinent to man Britain's buses and factories. The next one was made up of those

fleeing violence in Africa, Europe and the Middle East: Somalis, Afghans, Kurds. By 2004 the number of asylum-seekers had dwindled, but Britain was one of three EU countries to open its job market to workers from the European Union's eight new member states. So far perhaps 600,000 have shown up, though many have not stayed.



This diverse flood of newcomers has prompted much soul-searching about the merits of immigration. Pakistani doctors and Filipina nurses are a godsend to the National Health Service. Ubiquitous Poles are fixing wonky plumbing and computers, Lithuanians are picking broccoli and running translation firms, Estonians are providing excellent service in shops and hotels. The government reckons that as a group (which also includes American hedge-fund managers and Russian football-club owners) migrants are paying more in taxes than they are taking out in benefits. And some argue that an increase in young immigrants could help solve the pension problems of an ageing nation.

The micro picture is more nuanced. Immigrants have kept down wages, particularly for the low-skilled, and they are probably taking jobs from them too. The government is trying to get older natives to work for more years, and those on disability benefits to work at all, but employers will often prefer a young, healthy, keen foreigner. Small wonder that unemployment has increased along with employment. Immigrants are also pushing up house prices and piling into schools that had no chance to prepare for their arrival.

All this has meant that race and immigration have become Britons' top concern, according to IPSOS MORI, a polling firm. It is not that the country's immigrants and their descendants loom all that large: in the 2001 census only about 8% of the population defined themselves as belonging to ethnic minorities. The largest ethnic group, those of Indian origin, number 1m, and Muslims of any origin some 1.6m (France, by contrast, has 4.5m Muslims).

But ethnic minorities in Britain tend to be geographically concentrated: almost half live in London and most of the rest in other urban strongholds in the Midlands and the North. In the decade to 2001, their numbers grew by 50%. Leicester, in the Midlands, may be the first city to have an ethnic majority, within the next decade.

Britain prides itself on making newcomers feel at home. At Westminster 15 MPs are from ethnic minorities—fewer than their share of the population would suggest there should be, but there are more in the House of Lords. Representation in local government is much better. Cardiff's best delicatessen is run by Poles, and so is one of Dorset's best pubs. In east London's Brick Lane, Bangladeshis go to the Jamma Mesjid, a mosque that served earlier immigrants as a synagogue and still earlier ones as a Huguenot church.

There is strong evidence that the various communities are beginning to mix. Almost half of all Afro-Caribbean men in relationships have a white partner. Mixed-race Britons of all sorts numbered 674,000 in 2001. A-level English students last year were set “White Teeth”, an award-winning first novel about relations among immigrant communities by Zadie Smith, who is half-English and half-Jamaican.

London, which has one of the highest proportions of ethnic minorities, is relaxed about ethnicity and immigration. That may be because it is home to so many different groups. One person in 25 is of mixed race, and the number of incidents inspired by racial or religious hatred has fallen steadily for six years.

But there are also dramatic examples where multiculturalism has failed: repeated outbreaks of violence between blacks and whites, then Asian Muslims and whites, and then between blacks and Asian Muslims. That should not come as a surprise. Britain is one of the most crowded countries in Europe. There have been times when jobs for both immigrant and indigenous workers were scarce. The allocation of social housing to newcomers contributed to the uprooting of working-class communities and to the sense that immigrants' needs were being given priority. Most of the 200,000 or so who voted for the anti-immigrant British National Party in the local elections in May 2006 were members of the white working class who felt dispossessed.

Getty Images

The London terrorists' trial run

Earlier racial clashes in the 1970s and 1980s were thought to have sprung mainly from economic deprivation and unequal opportunities, with some reason. An Afro-Caribbean man is still more likely to go to prison than to university, says Trevor Phillips, until recently chairman of the Commission for Racial Equality. Many Pakistanis and Bangladeshis are at the bottom of the economic heap. But the educational gap between the different communities is closing. It is working-class whites who seem to be doing worst now.

Increasingly, however, racial clashes are seen as a sign of cultural alienation. An official report into the three-day battle between Asian Muslims and whites in 2001 in Oldham, a northern city, blamed it on a segregation so complete that the lives of the two communities “did not seem to touch at any point”. There are schools in London and Leicester where scarcely a white face is to be seen. A recent row over face veils exposed unease at what many see as growing separation within Britain.

The issue, say some, is not multiculturalism but Islam. Such generalisations are invidious. Britain's Muslims range from sophisticated professional people to simple village folk. Some Muslims shop at (or even own) Harrods, some run a corner store. Devout Muslims may follow Sufism, or Wahhabism, or neither; and some are no more observant than most Anglicans (ie, not very). Perhaps 14,000 are converts. And if there is one thing many of them have in common, it is a dislike of being classed mainly as Muslims, rather than as doctors, shopkeepers or just individuals.

Christian Britain has been a largely secular place for decades. But things are changing: when an employee of British Airways was denied permission to wear a small cross, squawks were heard across the land. BA prudently agreed to reconsider. Immigrants with more burning Christian convictions are pouring in, from Poland, the Philippines and Africa.

Sign of the crescent

As a group, Britain's Muslims come across as more disaffected than their co-religionists elsewhere. In polls an unusually high proportion identify themselves as Muslim first and British second, and younger folk are more likely to do so than their parents. They are also more likely than Muslims in, say, Germany or France to hold Western values in contempt.

This may be more of a reflection on Britain's foreign policy than its domestic policy. Images of British and American troops mowing down Muslims in Iraq and Afghanistan have alienated many. And since the terrorist attacks on America on September 11th 2001 police have been stopping and searching a disproportionate number of Muslims.

The bombs that exploded in London on July 7th 2005 shocked the nation not just because they left 56 people dead but also because among the bodies were those of four suicide-bombers from ethnic minorities who grew up in Britain. The video message left behind by their leader, Mohammad Sidique Khan, declaimed the grievances of Muslims in a broad Yorkshire accent.

Since then more news has emerged of alleged plots that were foiled. Mr Blair has given warning that the threat from home-grown Islamist terrorism will last for a generation. But what exactly motivates it? Not segregation, it seems. Ludi Simpson, a statistician at Manchester University, says that Muslims charged with terrorist offences are no more likely to come from heavily Muslim areas than from whiter ones. Nor do they seem especially poor.

For over a decade critics in Washington and Paris have been accusing Britain of protecting dangerously radical clerics. Since 2001 some of Mr Blair's toughest—and mainly unsuccessful—parliamentary battles have been over measures to tighten security by limiting the right to free speech and prompt trial. Threatened or not (and perhaps earlier experience with the IRA has created a certain robustness in the face of terrorism), Britain is a liberal country not easily shaken from its beliefs.

Many are now wondering whether Britain has struck the right balance between encouraging cultural diversity and insisting on a shared national identity. Yet in order for minorities and majority to accept a common identity, there must be a clear idea of what it means to be British, and that is lacking. “When we were an imperial power, the main industrial nation in the world, defining our identity didn't matter,” says Mr Brown, Britain's prime minister-in-waiting. “Now it does.”

Britain has always been a union of nations. That may be one reason why multiculturalism came easily to it. But with devolution, the Scots and Welsh are becoming keener on their more local identities (see article) and less interested in being British. Mr Brown has long argued for a new definition of Britishness around which the country's different peoples could unite. This identity, he says, should consist of shared values such as decency, tolerance, fair play and the rule of law.

The trouble is that although this tolerant rule-abiding society does exist, it is not always visible to Britain's minorities. They are understandably dismayed, for example, by the behaviour of Britain's young, who are statistically the worst-behaved in Europe on an wide range of measures.

So what identity might a more united Britain strive towards? The chances are that one will evolve spontaneously, if at all. But education is bound to play a part in it. It is not just a question of teaching British history in a clear and inclusive way, but of improving education across all subjects. The higher the quality of education, the more likely the different groups are to blend. Polls suggest that highly educated people tend to be more open and less prejudiced. They are also likely to earn more money, which gives them more choice over where to live.

Mr Blair, the man who has helped to shape British identity for nearly a decade, is preparing to step down. So what will Britain be like when he has gone?

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The rose and the thistle

Feb 1st 2007
From The Economist print edition

Not forgetting the leek and the red hand

Get article background

THE question of identity is complicated by more than just immigration. As globalisation and groupings such as the EU make nation states grow weaker, smaller units command more loyalty.

January 16th was the 300th anniversary of the Act of Union between Scotland and England, when not only the crowns but the countries were joined. Despite the (muted) celebrations, regional elections due on May 3rd are likely to show the strongest support yet for breaking up Great Britain.

In 1998 the freshly elected Labour government in Westminster transferred limited autonomy to Scotland in response to a rising tide of nationalism there, and even more limited powers to a somewhat less nationalist Wales. The idea was to give separatists some of what they wanted and thus preserve the Union.

Yet an ICM poll in November, and others since then, have found that more than half of the Scots questioned favour an independent Scotland. Support for the Scottish National Party (SNP), which advocates independence, outstrips support for the Scottish Labour Party, now ruling with the Liberal Democrats.

This does not mean that Scotland is about to say goodbye to an annual subsidy of about £1,300 per Scot from the central government at Westminster and walk out. “Independence” can mean different things to different people, and discontent may have more to do with the way the limited devolution has worked so far and with Labour politicians both at Holyrood, the seat of the Scottish parliament in Edinburgh, and at Westminster.

The problem for Labour is that it cannot win Britain without Scotland; and more English folk seem to be noticing that Scottish members of Parliament at Westminster get to vote on matters affecting England, whereas English MPs no longer vote on matters affecting Scotland. The West Lothian Question, as this is arcanely known, has no simple solution.

In Wales few want full-fledged separatism, but devolution has grown popular. In the 1997 referendum a bare majority was in favour, but in a recent survey the Welsh agreed by a healthy margin that devolution had improved the way their country was run. Now there is pressure to shift more powers to Cardiff.

Nationalists all

The strangest development is the growing strength of English nationalism. The English used to be a laid-back lot with no interest in a separate assembly. But the same November poll that found a majority of Scots for Scottish independence also found nearly half of English people supporting independence for England.

In Edinburgh and Glasgow it is easy to see that devolution has put a spring in people's step. Glasgow has become Britain's third most popular tourist destination, after London and Edinburgh, and is building up a base of financial firms. The two cities are even toning down their long-standing mutual animosity.

Cardiff is less ambitious, and friendlier. Its residents would particularly like a convention centre to get in ahead of Bristol. But Wales has recently managed, against stiff competition, to attract IBM to a £50m development at the Institute of Life Sciences at Swansea University. Rhodri Morgan, the first minister for Wales, notes that this is the first time a leading global technology firm has come not to manufacture or assemble but to develop intellectual property in Wales.

And then there is Northern Ireland, where devolved government has been in suspension since 2002. The road to resolving the centuries-old struggle between Catholics and Protestants has been long and rocky, with unpalatable compromises along the way. A deal now looks likelier, if only just. Great credit is due to Tony Blair for persevering.

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The changing of the guard

Feb 1st 2007
From The Economist print edition

How Brown's Britain will be different from Blair's

PRIME MINISTERS do not usually hand in their house keys. From the moment when Mr Blair announced that he would not lead his party into a fourth election, the only question that mattered was when he would leave. Since then power has ebbed from Labour's most successful prime minister towards the man who thinks he should have had the job all along.

The partnership between Mr Blair and Mr Brown—brothers in political arms from their early days in Westminster, then rivals for the top spot—was always odd. That it worked at all, let alone lasted for ten years in office, is remarkable. For all the rivalry, the two broadly shared a view of what needed doing, both at home and abroad. So although Mr Brown was in charge of economic policy, Mr Blair of foreign policy, and the two overlapped on many matters at home, Mr Brown is unlikely to do anything very different from the man with whom he co-authored New Labour.

Mr Blair's big domestic idea, when he got round to articulating it, was investing in and reforming Britain's underperforming public services. Customer choice—of schools and hospitals, for example—was to encourage competition and improve standards. He lavished money and effort on education and health, rarely pausing long enough to see if the last lot had worked.

In foreign policy, Mr Blair began by balancing Britain's two key alliances more carefully than either of his two immediate predecessors. He engaged enthusiastically enough in EU matters to claim with some plausibility that Britain would be “at the heart of Europe”, at least until Dutch and French voters turned down the prospect of a European constitution and let him off the hook. At the same time he managed to create a close working relationship with Bill Clinton and later with George Bush.

What upset that balance, more than anything, was the invasion of Iraq in 2003. This decision, opposed by Britain's third party, the Liberal Democrats, hijacked his reform agenda along with his domestic popularity. He may have believed passionately in the cause, but the intelligence on which he sold it to the nation was wrong. And as the aftermath of war turned ever bloodier, there was a growing sense that Mr Blair's foreign policy had ceased to serve British interests.

Mr Brown is not yet beyond challenge. But assuming that he succeeds Mr Blair, perhaps in June or July, what difference will that make to the way Britain is governed? Much of the debate turns on his style and personality.

For most of his time in office Mr Blair was a popular leader. He has the rare gift of being able to speak naturally and even intimately to the masses. Mr Brown, by contrast, can come over as craggy and brooding. His friends say he is great fun in private, but he does not convey warmth or ease to the electorate at large. His brains and tenacity are widely noted, along with the fact that opponents rarely get the better of him. When Charles Clarke, home secretary until May 2006, called him a “control freak”, few disagreed.

But the chancellor comes with an important hinterland. He has a sense of the sweep of history and of the institutions on which the nation is built. He feels tribal loyalties—to Scotland, to Old Labour—which the temperamentally inclusive Mr Blair lacks. That creates some awkwardness. Mr Brown's son-of-the-manse Scottishness is an essential part of who he is. That was no drawback for a chancellor but may be for a prime minister.

As for the Old Labour associations, the chancellor is no closet left-winger. Yet his desire for equity is more pronounced than Mr Blair's, who sees little wrong with wealth as long as everyone can have a bit of it. He is a tinkerer, too, which is one reason why even businessmen who approve of his economic management have reservations about him. And he may be less committed than Mr Blair to unleashing competition in public services.

But Mr Brown is certainly a champion of globalisation. “I come from Kirkcaldy in Fife where Adam Smith wrote 'The Wealth of Nations'. I know the place where he was born and brought up. He saw a hundred ships coming in every year and saw that trade held, through the division of labour and specialisation of labour, the key to future wealth and prosperity,” says Mr Brown. So as prime minister would he move Britain up the competitiveness league tables?

Mr Brown has correctly identified many of the things that need to happen if Britain is to hold its own in the world: productivity and skills must be improved,

PA

entrepreneurship and innovation should be encouraged. Yet such matters are not susceptible to a quick fix, and as prime minister he will have little more power in these areas, except perhaps in education, than he has had for a decade as chancellor. What is within the government's control is taxation and regulation, and on this count Mr Brown has been a nuisance.

The tricky bit for Mr Brown as prime minister will be to find some way of differentiating himself from his predecessor. That will be hard, because Labour has had its revolution and Mr Brown was at the heart of it. Oddly, his best chance of success may be in the area where he is seen to be least experienced.

Mr Brown rallies the troops

Cabinet colleagues say Mr Brown was opposed to going into Iraq, which will prove useful as he tries to draw a line under the past. And he has made it clear that he intends to take a more independent line with America. Mr Brown, like Mr Blair, sees the relationship as resting on shared values. He is an instinctive Atlanticist, and though he may not be a natural soulmate of Mr Bush's, he knows that he will not have to cultivate him for long. Besides, Mr Brown is no sandal-wearing pacifist: he was quick to back replacing Britain's independent nuclear deterrent. But there will be a change of tone. Whereas Mr Blair sees Britain's role as a bridge between America and Europe, for Mr Brown Britain is not so much a bridge as a beacon, for example in areas such as foreign aid.

Closer to home, Mr Brown is less Europhile than Mr Blair, but then the EU has changed too. The European Commission is now run by José Manuel Barroso, a liberal, pragmatic Portuguese, and the new member states are more inclined than some of the older ones to admire America and favour free markets. But a new attempt to revive parts of the defeated EU constitution has just been launched. Ceding sovereignty to Europe is a political hot potato in Britain. It could be awkward for Mr Brown as the country moves towards its next general election, which is due by May 2010.

The biggest difficulty for Mr Brown is that just as one great communicator in his life is moving offstage, another one is attracting the spotlight. David Cameron, who celebrated his first anniversary as Conservative leader in December, is not yet a Tony Blair, but he has the same ease, the same ability to speak as if he means it, with just a sprinkling of glamour. And he has clearly drawn lessons from how Mr Blair made his party electable.

Mr Cameron's biggest error to date has been his decision to take Tory members of the European Parliament out of the main centre-right grouping and establish a more Eurosceptic alliance. When respectable allies proved hard to find, he postponed the move. Europe remains a bitterly divisive issue within his party. The Tories' relations with America, by comparison, are straightforward and for the most part cordial.

“The tragedy of the last ten years”, says Mr Cameron, “is that we had strong economic growth from 1993 and could have made ourselves the Hong Kong of Europe, with low taxes and reformed education. We missed the chance.” But it is not clear that, given the opportunity, he would pursue policies that are all that different from Mr Blair's or Mr Brown's.

Crowded middle ground

And that, in a sense, is Mr Blair's lasting legacy. New Labour's particular blend of free-marketry and social justice is now widely seen as the natural path of British politics, and few politicians of any stripe would dare to veer far from it.

Mr Brown dismisses Mr Cameron as a lightweight, but has some reason to fear him. Polls in January showed the Tories leading Labour by five to seven points. That may not be enough for them to win the next election outright, but it puts them in with a chance.

If neither party wins an overall majority, the balance will be held by Britain's third party, the Liberal Democrats, led by Sir Menzies Campbell. As the two main parties have scrambled for the centre ground, the Lib Dems have emerged as the real opposition on issues such as Iraq and civil liberties. The last time the Liberals were part of government was during the Lib-Lab pact of 1977-78. At that time a Liberal-Conservative alliance would have been unthinkable. But if Mr Cameron gets more votes than Mr Brown, the Lib Dems will have to put their thinking caps on.

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Full steam ahead

Feb 1st 2007
From The Economist print edition

What Britain must do to maintain its momentum

THE man in Victorian London's street was in favour of open markets, and his descendant today still shares his instincts. In a survey last year by the German Marshall Fund, a think-tank, respondents in Britain supported freer trade, approved of foreign direct investment and valued the contribution of immigrants in greater numbers than those in other big developed countries (see chart 6).

International integration has brought Britain huge gains in the form of lower prices and interest rates and greater prosperity all round. These benefits are hard to quantify, but America's Peterson Institute for International Economics puts the bonus from globalisation in that country at over $1 trillion, or almost 10% of GDP. In an economy such as Britain's, which is more open to the outside world, the advantage is likely to be even bigger.

Nor is the effect only economic. Britons' lives have been vastly improved by the availability of affordable foreign goods, from food and clothing to films, as well as by an influx of people to challenge their insularity and greater opportunity to travel and live abroad. But, allied with technology, globalisation has also brought strains, through dislocations in the job market, pressures on social services and a trend towards greater inequality.

There is nothing to say that globalisation will continue indefinitely. The previous wave ended in war and depression in the early part of the 20th century. What could make it fizzle out this time?

Enemies of promise

One possibility is a surge in terrorism, another the growing concern over global warming. A third might be a backlash against globalisation among people in rich countries. Britain was less keen to admit workers from the latest EU entrants, Bulgaria and Romania, than from countries that joined earlier. And the Doha round of world-trade talks has stalled.

A fourth risk is resurgent economic nationalism as countries such as Russia and China—and indeed America—race to secure and exploit scarce raw materials. The German Marshall Fund survey also showed a strong drop since 2005 in the share of respondents, particularly in Britain, who believed that globalisation was likely to lead to world stability and peace.

But it is getting harder to stop international economic integration, because at each stage of the production process firms are more intertwined than they were. And business done over the internet cannot easily be policed.

Globalisation does not mean the end of nation states, though it does restrict their freedom of action. Governments still have an important role to play: they must invest in things that improve productivity—eg, transport, health and education—but they must do so effectively or risk overburdening their citizens with taxes.

“What we need to do on skills, productivity and enterprise is fairly obvious,” says Mr Blair. “We just need to get on and do it.” Of this trio, skills are the most important and, in time, most likely to have a beneficial effect on the other two. A coherent, high-quality education system is not only the way to hone the competitive edge that a country living on its wits is going to need. It also offers the best chance to bring together disparate communities and let them develop a common identity. Perhaps reassuringly, Mr Brown recently declared education to be his main priority (though Mr Blair said the same when he started in his job, and has produced mixed results).

Can Britain go on doing as well as it has done in the past decade? “The genius of England is universally admitted to be of an eminently enterprising and speculative character,” maintained *Once a Week* magazine, a popular Victorian rag. In the 19th century its enterprise produced splendid results. The wind in Britain's sails slacked off a bit after that, but it has picked up again in recent years. From the reinvigorated City of London to innovators like Sir James

Dyson, there are plenty of signs that Britain can be creative and successful, “as long as we get things right,” as Mr Brown puts it. Let us hope that he can.

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Business in Russia

Dancing with the bear

Feb 1st 2007 | MOSCOW
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Alamy

Want to make money in Russia? Here are some ground rules

AS A parable of the quirks of doing business in Vladimir Putin's Russia, the tale of the confiscated mobile phones is hard to beat. Last year 167,500 Motorola handsets were seized on arrival at a Moscow airport. They were variously alleged to be smuggled and counterfeit; to violate a Russian patent; and to be a danger to public health. Around 50,000 phones were supposedly destroyed by the interior ministry—though some were later said to have turned up on the black market.

Eventually, most of the handsets were returned: evidence of progress or chaos, depending on your point of view. But the moral of the story lies in the fact that Motorola's enthusiasm for Russia is undimmed. Sergei Ovcharenko, the firm's country boss, says Russia is now the world's third-biggest handset market, after America and China. Since they “tend to spend more on demonstrating what they can afford”, many Russians opt for snazzy models. Motorola's sanguine attitude is shared by many multinational companies. For all the risks, there is a striking dissonance between the growing Russophobia of politicians and the enthusiasm of investors.

Bullying foreign policy and human-rights abuses are not all that have tarnished Russia's reputation. Under Mr Putin, the Kremlin has scored an unfortunate hat-trick of business scandals. Most of what was once its top oil company, Yukos, has been expropriated, its founder dispatched to a Siberian labour camp and its other shareholders cheated. Bill Browder of Hermitage Capital Management, the boss of the biggest portfolio investor in Russia, has been shut out of the country, ostensibly because he is a threat to national security, but probably because of his scrutiny of Russia's murky corporate governance. And state-backed racketeering has helped Gazprom take charge of an oil-and-gas project on Sakhalin Island, Russia's largest foreign direct investment (FDI) scheme. TNK-BP, an Anglo-Russian oil firm, may be the next big victim.

Yet alongside these high-profile scandals, Russia's economy has grown strongly for eight years, and by just under 7% last year. The Russian contingent at the World Economic Forum in Davos last week bragged that their country's GDP would soon overtake that of France. Rising oil and gas production and sky-high prices have driven that growth, but sound macroeconomic management—Mr Putin's most unequivocal achievement, which has seen debt paid off and much of the oil windfall stashed in a rainy-day fund—will insulate the economy from a falling oil price, for a while. Salaries are rising fast, most Russians save little and consumer credit is increasingly available even for small purchases, such as flashy mobile phones.

All that, plus the rouble's strength against the dollar, means big profits can be made in financial services, construction, and especially consumer goods and retail, where sales last year grew by 13%. Top money-spinners include groceries, beer and cars. PricewaterhouseCoopers, a consultancy, says new foreign cars (many assembled in Russia) outsold domestic brands for the first time last year. Russians have learnt that foreign brands can offer better value even at high prices, as well as conferring status. And they are demanding as well as aspirational: Erik Sandberg, formerly of Cadbury Schweppes, a confectionery and drinks firm, says its Russian call centre receives the most sophisticated questions anywhere.

Consider the experience of that global totem of middle-class consumption, IKEA, which has spent $2.4 billion in Russia. It now has eight stores and runs eight mega-malls. “Russia is a bit of a rollercoaster,” says Per Kaufmann, its local boss, with Scandinavian equanimity. “You don't know exactly what will happen tomorrow.” Like many others—PwC was accused of tax evasion this week—IKEA has had run-ins with the authorities. Its Nizhny Novgorod mall recently had to close for ten days, allegedly for fire-safety infractions, but possibly for murkier reasons.

Yet the widespread and lucrative Russian urge to trade up from Soviet furnishings evidently justifies the hassle. Sofa-beds, slippers and vodka glasses are local favourites. Mr Kaufmann says his Russian staff are quick learners: half his store managers are locals. Reflecting the spread of prosperity beyond Moscow, five of IKEA's stores are outside the capital, and three more are to open this year. Mr Ovcharenko reckons Moscow now accounts for around a quarter of Motorola's Russian sales, with three-quarters elsewhere: a reverse, he says, of the situation a few years ago.

Last year, even as Mr Putin and his Western counterparts became ever more estranged, the Russian stockmarket boomed, and FDI reached around $30 billion—twice as much as in 2005, and less concentrated than before in oil and gas. Big risks such as political upheaval, which might deter investors, seem reasonably remote. One of the economic braggarts at Davos was Dmitry Medvedev, a deputy prime minister who is the favourite to succeed Mr Putin in 2008, and whom many investors regard as the least bad candidate.

Even if they are sometimes obliged to make “voluntary” contributions to the local community (for example, by paying for new fire engines), multinationals are less vulnerable to the everyday risk of extortion by corrupt officials and police, which many Russian businessmen say has worsened under Mr Putin. Multinationals also stand a better chance of defending themselves in Russia's dodgy courts. The main worries at the moment concern crazy red tape, counterfeiting and rising wages.

So what are the rules for safe success in Russia? First, avoid industries that the government considers “strategic”, such as natural resources—but remember that the government is liable to change its mind. (A long-awaited set of new laws may soon define the rules for foreign firms in these areas.) Second, avoid the wrong sort of partner: steer clear of the “oligarchs” who made shady fortunes in the 1990s, and anyone too close to Mr Putin, since his fortunes may change after 2008.

Third, make the right friends, which in the regions means buttering up the local governor. Mr Ovcharenko says it's important not to appear to be a fly-by-night profit-stripper. “The more you invest, the safer you are,” he says. Be big enough to defend yourself against bureaucratic attacks, but avoid irking rivals with better connections. Finally, be ready to hold your nose when elections are rigged and political opposition is crushed.

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Indian retailing

Getting cheaper and better

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But foreign firms must walk while locals run

RARELY can so many people have gathered for an advance look at a medium-sized grocery store. Then again, few shops have inspired such extravagant dreams as the convenience stores being opened across India by Reliance Industries, an oil, petrochemicals and textiles group. The new shops are among the first approximations to a supermarket in India, which has over a billion people and virtually no organised retailing.

Reliance opened nine shops in and around Delhi on January 30th, including its showcase example in the nearby town of Noida. They are the first of their kind in India's capital, supported by a "farm-to-fork" logistics chain, which is supposed to guarantee quality and supply. This week's openings took Reliance's tally to 55 shops in three months, under the name Reliance Fresh. Others have opened in Chennai, Hyderabad, Jaipur and elsewhere. Reliance intends to open 100 stores in Delhi alone by April. In India as a whole it plans to invest 250 billion rupees ($5.7 billion) in 5,000 shops, including larger hypermarkets, the first of which will open in June and will be up to 20 times the size of today's outlets. By 2010, the group hopes to have annual sales of $25 billion.

That is realistic, given the vastness of Reliance—it is India's biggest private-sector company—and of India's retail potential. For foreign companies, until recently forbidden to invest in India's retail industry, the prospects are mouth-watering. After 15 years of decent economic growth, averaging over 8% in the past four years, India's masses have cash to spend. India has over 12m retailers, employing more people than any industry except agriculture. That is a mark of a huge demand, especially for staple foods and cheap household items, but also of inefficiency. Around 97% of India's sales are in small, often family-owned shops, where the quality and availability of goods is unpredictable.

Reliance is not alone in trying to muscle in on these shops' business. There are already a few national Indian retail chains, including Pantaloon, India's biggest retailer at the moment. And a few foreign firms have taken 51% equity stakes in shops that sell only their own brands, taking advantage of new rules introduced last year. Further foreign investment is expected after a recent decision to allow foreign firms to establish wholesale operations. This has led to a series of joint ventures in which Indian retailers will be supplied exclusively by foreign wholesalers. One such agreement, between Bharti Enterprises and Wal-Mart, is said to have won approval from the government last week. Carrefour, the world's second-largest retailer, which also discussed a partnership with Bharti, is rumoured to be talking to other firms.

Yet Indians remain suspicious of foreign direct investment generally, and in retail especially. They fear for the fate of the 12m "unorganised' retail outlets, as the family-type shops are technically called. Reliance knows this. At the launch in Delhi, Raghu Pillai, the head of Reliance Retail, claimed that the new shops would create half a million new jobs in three years and would cause practically none to be lost—a Utopian scenario. He also promised that small shopkeepers would be able to buy from Reliance on a wholesale basis, and so benefit from its supply chain. That shoppers will benefit seems more certain. In a brief survey of established grocers in Delhi, your correspondent's cook found Reliance's prices extremely competitive—especially for green beans and onions.

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Business in southern Italy

Taking on the mob

Feb 1st 2007 | GIOIA TAURO
From The Economist print edition

A farming co-operative defies the Calabrian Mafia

DECEMBER 20th was a normal working day in the large container-port at Gioia Tauro in Calabria. It was also a normal working day for the *'ndrangheta*, the Mafia that rules the region. Mafiosi broke into the workshop of the Cooperativa Valle del Marro, about five miles inland, stole equipment and damaged machinery. Established two years ago by a group of young people, the co-operative is the first firm in Calabria to seek to establish a legitimate business using assets that were once owned by the Mafia. The cause of the break-in was the co-op's audacity to farm land that, until its confiscation by the courts, had belonged to the Piromalli family, the most powerful around Gioia Tauro.

The co-op's members pulled out citrus trees from long-neglected orchards, prepared the land to plant crops and last spring harvested their first chilli peppers and aubergines for bottling in extra-virgin olive oil obtained from olive groves, also confiscated from mafiosi, ten miles away in Oppido Mamertina. A left-leaning co-operative group helped with a grant of €50,000 ($65,000), Tuscan organisations donated machinery and members put in cash. Even so, finance is a problem. Monthly pay is about €1,000 and several of the co-op's members work unpaid.

Banks are reluctant to lend money, since the land belongs to the state and the co-op lacks assets to pledge in guarantee. Despite these difficulties, and the authorities' lukewarm support, the co-op successfully launched its first products last July, emphasising their anti-Mafia credentials. The break-in at Gioia Tauro, which was accompanied by sabotage at Oppido Mamertina, was a blow. “The risk of further attacks will increase after we have planted in April. Poisoning and uprooting are easy,” says Giacomo Zappia, the co-operative's chairman.

The co-op will soon be even more vulnerable, since it plans to double the cultivated area to 14 hectares and increase its productive olive groves to 43 hectares. Unlike the nearby container-port's high fences, with their barbed wire, armed guards and anti-intruder technology, the co-operative's boundaries are easily breached. More than others in Calabria, Mr Zappia's firm is in the front line.

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Dell

Return to founder

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Michael Dell returns to the helm of the company he founded

THE computing world has traditions, if not clichés. It is, for example, customary for the founders of big technology firms to have dropped out of college, or at least graduate school, before getting started. Everyone from Steve Jobs (Apple), Bill Gates (Microsoft) and Michael Dell (Dell) in the industry's first generation to Larry Page and Sergey Brin (Google) in the current one has so far complied. If you absolutely cannot start your company in a garage, as Bill Hewlett and Dave Packard (HP) did long ago, and Chad Hurley and Steve Chen (YouTube) did more recently, then at least launch it in your dormitory room just before dropping out—as Messrs Dell, Page and Brin did. And once a company loses its youthful vigour, it behoves the founder to leave, watch it suffer, then return as saviour. Steve Jobs did so with great effect; Gateway's founder tried too. This week, Michael Dell decided that it was his turn.

Since founding Dell in 1984, he has never actually left—he has been chairman throughout. But in 1996 he brought in Kevin Rollins, a consultant at Bain who had become part of Dell's management in all but name. For eight years Mr Dell promoted and groomed him as his heir-apparent. These were good years, during which Dell became the world's largest and most profitable computer-maker, with a supply chain that was easily the most efficient in the industry, if not the world, and a direct-sales model that seemed to keep Dell one step ahead of rival companies selling computers through old-fashioned stores.

But when Mr Rollins finally took over as chief executive in July 2004, things started to go wrong almost immediately. At first Mr Rollins, a reticent Mormon and teetotaller who plays the violin, looked disciplined compared with Carly Fiorina, the flamboyant boss of HP, Dell's main rival, and Dell continued to trounce HP in the market. But then Ms Fiorina was fired by her board, and replaced by Mark Hurd, whose collars look as starchy as Mr Rollins'. Dell soon began losing market share to HP, and even suffered the ultimate ignominy: falling profits. Its cost control had gone too far, and customers caught in the endless phone menus of Dell's support centres frequently broke down in tears.

It kept getting worse. Last year a newly focused HP displaced Dell as the world's largest computer-maker. Videos of a burning Dell laptop computer were all over the internet, and Dell had to recall 4m of the things (the blame belonged to Sony, which had supplied faulty batteries, but the brand visible under the flame was Dell's). Then America's securities watchdog began investigating Dell for accounting problems, probably relating to revenue recognition, and Dell may yet have to restate profits for the past few years.

Mr Rollins clearly bears most of the blame. He waited far too long to include microprocessors from AMD alongside those from Intel in Dell's products. He missed the even bigger trend, set by Apple and followed by HP, of computers becoming entertainment devices, and thus works of art to be fondled in stores before a purchase. Dell remained grey, dull and reachable via the web and a toll-free number.

Mr Dell stuck up for his friend for a long time. Just as they shared the credit when times were good, they should now share the blame, he said. (Their offices were separated only by a glass door, apparently never closed). But Wall Street, livid about the falling share price, kept complaining, and Mr Dell had to act. As the new chief executive, he says he will try to move into high-margin services, and will consider tweaking the sacred direct-sales model.

Pundits and investors are overjoyed. Mr Dell's return, says Mark Anderson, who publishes an influential industry newsletter, “should almost immediately elevate Dell back to the performance levels it has historically enjoyed.” At least, that is what the industry's folklore demands.

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Motorola

Uh-oh, Moto

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Carl Icahn takes an interest in struggling Motorola

IT MAY come to be seen as the Motorola shock. The world's second-largest maker of mobile phones seemed to have been restored to health last year, thanks to its RAZR and other slimline handsets. But it stumbled badly in the last three months of 2006. In January it said its operating profits had fallen by 56% in the quarter compared with a year earlier, and operating margins had narrowed sharply. And this week the pressure intensified on Ed Zander, Motorola's boss. Carl Icahn, a renowned activist investor, said he had taken a 1.4% stake in the company, and demanded that Motorola start disgorging cash to shareholders.

Although Mr Icahn is an unsolicited caller, Mr Zander should listen carefully to his message. He should also consider what happened to Sony, Japan's electronics-and-media giant, after its earnings and shares suffered a similar collapse in 2003. As with Motorola, falling margins for core products were the proximate cause of the “Sony shock”. What really hurt Sony, however, was the unimpressive way in which it responded. Sony had long espoused vague ideas about exploiting the convergence between previously separate digital devices and forms of media. After the shock, investors asked tougher questions about how this would work. The more they asked, the clearer it became that Sony's boss at the time, Nobuyuki Idei, did not have an answer.

Motorola is in a similar pickle. Its sliding performance stems mainly from falling margins for mobile handsets, its core products. The iconic RAZR, launched in late 2004, enabled the company to increase its margins and gain market share. When Motorola followed up last year with the KRZR (a narrower version of the RAZR) and the Q (a slim phone with a keyboard for e-mail), it reassured sceptics who worried that the RAZR's success had been a lucky one-off. But the industry moves fast, and rivals have responded with their own slim models. Worse, Apple is entering the market with its first handset, the iPhone. Brian Modoff, an analyst at Deutsche Bank Securities, says Apple has produced something truly new, whereas Motorola is merely making incremental improvements.

As Motorola's handset business adjusts to these threats, however, an even bigger difficulty facing Mr Zander is how to handle questions about Motorola's other businesses. Like Sony's Mr Idei, Mr Zander likes to talk about convergence, and how his company will benefit from it by investing in whizzy new technologies such as internet-protocol TV and WiMax. Although he has made a few acquisitions to bolster this strategy, it is still rather vague. Mr Icahn wants him to return much more of Motorola's $11.2 billion cash pile to shareholders. To reject this suggestion convincingly, Mr Zander will have to start articulating his strategy with much greater clarity.

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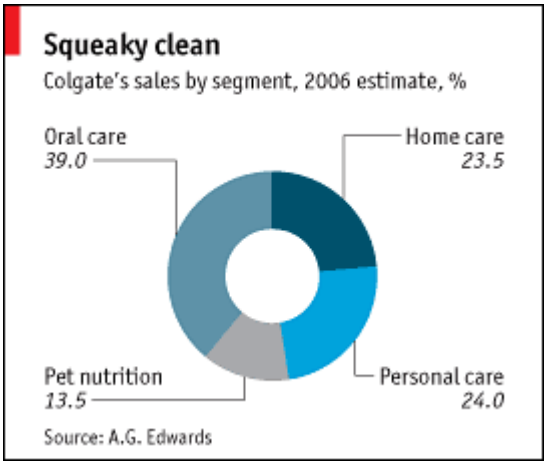
Colgate-Palmolive

Still fresh?

Feb 1st 2007
From The Economist print edition

Colgate's days of rapid growth may now be behind it



FEW chief executives nowadays manage to dominate a company for as long as Reuben Mark has, let alone leave at a time of their own choosing and with an intact reputation. Mr Mark, who confirmed on January 30th that he will step down as boss of Colgate-Palmolive this year (probably at the annual meeting in May, say analysts) has headed the consumer-products giant for 23 of his 68 years and worked there for more than 40. During his tenure total shareholder returns have exceeded 4,000%, almost three times those of the American stockmarket. This week Colgate announced record profits of $1.65 billion (£897m), up 12% over 2005, on sales of $12.2 billion—and promised further double-digit growth for 2007.

The higher the note on which Mr Mark departs, however, the tougher the job will be for his successor, Colgate's 54-year-old president and chief operating officer, Ian Cook. The impact of a big restructuring programme (a rare event at Colgate) which helped to lift profits last year, and should add some $300m to the bottom line in 2007, will fade thereafter. Rapid expansion in Latin America, which accounts for nearly a third of profits and where sales are growing by 14% a year, may slow as the region's economies cool. Some analysts expect Colgate's earnings growth to drop to the mid-single digits from 2008.

It is hard to see what could rev it up again. The legacy of Mr Mark's disciplined and highly focused style is a culture that is conservative—some would say overly conservative. Colgate's last big innovation, its range of “Total” toothpastes to fight tooth decay, was introduced in the 1990s. It was late to the newer craze for whitening strips, which was spotted first by Crest, its arch-rival, owned by Procter & Gamble (P&G). Colgate's copycat product—a paint-on whitener—was a flop. And most of Colgate's recent new products, though slickly promoted by celebrities such as Brooke Shields, are brand extensions: toothpastes flavoured with mint or cinnamon, or enriched with vitamin C.

“Colgate is not strong on big innovation,” says Jason Gere, an analyst at AG Edwards in New York. “The business is in great shape now, but my biggest question is about future growth.” By contrast, P&G has gambled on entire new product categories and has created billion-dollar hits such as its Swiffer anti-static mops.

In addition to its relative lack of innovation, Colgate has also eschewed big acquisitions. Mr Mark reportedly once dreamt of a merger with Gillette, a company snapped up by P&G in 2005. Last year Pfizer's consumer-health division, including Listerine mouthwash—a brand Mr Mark said he would love to own—was bought by Johnson & Johnson. Either multi-billion dollar deal would have been risky. But by passing them up, Colgate has closed off potential routes to long-term growth and allowed two of its larger rivals to become even more threatening.

Once P&G combines the clout of its own Crest brand with Gillette's Oral-B franchise, Colgate could find its core earnings from toothpaste being squeezed. And Colgate's heavy reliance on a few categories (it is in about one-fifth as many product markets as P&G) in a relatively small number of regions (in some Latin American countries its market share in toothpaste approaches 80%) makes it vulnerable to a price war or a determined marketing push by a rival.

Today such risks look theoretical, and Colgate's healthy near-term growth and fat share-price are very real. Yet corporate fortunes can change rapidly and it is worth asking how quickly a culture as conservative as Colgate's would adapt. Mr Cook is a reserved, rather unflamboyant British marketing manager, making Mr Mark look feisty by comparison. Like Mr Mark he is also a company lifer, having been at Colgate for over three decades. Not only has he risen under Mr Mark, he will also have his former boss remaining as chairman, at least for a while—which falls short of best practice in corporate governance. The rest of the board of eight non-executive directors has an average age of more than 66 (three are over 70) and six have each served for more than 10 years—which under British standards would throw their independence into doubt.

Investors rarely question a company's corporate governance when all is going well, but they swiftly turn into critics if

things change. Mr Cook is inheriting a strong, efficient company, but maintaining Colgate's growth will be no easy task.

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Feb 1st 2007
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Adam Tinworth

Has Tariq Krim created a French internet blockbuster?

"IF FRANCE was more like Netvibes, things might be a lot better here," says Tariq Krim, with disarming frankness. The website, which he runs out of Paris, is the most popular of a new class that lets users snap together individual components such as blog feeds, e-mail accounts, news headlines and videos to create a "dashboard", or home page, that displays all their online information. If only his country—with its grand projects, restrictive labour rules and social hierarchy—showed similar flexibility, laments the 34-year-old Frenchman. Politicians on the stump seem to agree. Having snapped together journalism, business ventures and politics in his own career, Mr Krim is now cast as a paragon of Europe's new generation of internet entrepreneurs.

The son of well-to-do Algerian immigrants, Mr Krim grew up in the Marais, a chic Paris neighbourhood. He was given a computer at the age of nine, and by the age of 12 he was cooking up his own software for Minitel, France's national data network, which predated the web. In secondary school he insisted on being taught English with an American accent, corresponded with an American pen pal and spent a few weeks as an exchange student at a high school in New York. After completing his studies in engineering at ENST in Paris, one of France's *grandes écoles*, he went back to America for an internship at Sun Microsystems, a computer-maker that was expanding fast as the internet took off.

Mr Krim duly caught the internet bug, but instead of becoming a computer engineer, he began covering the internet for *La Tribune*, a business newspaper. "At the time, few journalists in France knew the internet and many distrusted it," says Paul-André Tavoillot, his boss at the time. Mr Krim felt his countrymen were not taking the new technology seriously, and wanted to do something about it. "In France the internet is a gadget," he says. "In America the net is a real industry." One day in 1999, while interviewing an executive from an online-music start-up at an internet conference in San Francisco, Mr Krim changed tack yet again. "What am I doing?" he remembers asking himself. "I'm on the wrong side of the interview."

So he launched a site called mptrois.com, which grew into GenerationMP3.com, a popular network of French music blogs. The inspiration for Netvibes came to Mr Krim one day as he was trying to track the activity on all his blogs. To save himself having to click from one to the next, he used "Web 2.0" programming tricks to enable him to oversee all his blogs from a single page. Backed by angel investors including Martin Varsavsky, an Argentine-Spanish entrepreneur, and Marc Andreessen, co-founder of Netscape, Mr Krim turned the tool into a business. Launched in September 2005, Netvibes attracted 15,000 users on the first day and has since grown quickly: the number of users is expected to exceed 10m this month. Last August two venture-capital firms, Accel Partners and Index Ventures, invested €12m ($15.4m) in the company. Originally launched in English and French versions, Netvibes has since been translated by volunteers into 50 other languages, including Chinese, Spanish, Hindi, Russian and even Catalan and Basque. So far the firm has relied entirely on word-of-mouth promotion by its fervent adherents to attract users.

France's politicians have also noticed Netvibes, and have courted Mr Krim. Speaking in December at a conference in

Paris, Nicolas Sarkozy, the centre-right candidate in France's forthcoming presidential election, cited him as one of the country's examples of “exceptional talent” in the internet realm. Not to be outdone, Ségolène Royal, Mr Sarkozy's Socialist rival for the presidency, is using Netvibes to distribute news about her campaign.

Since the grim blocks of Paris's *banlieues*, best known for the car-burning riots of 2005, are far from Mr Krim's *soigné* background, he has resisted attempts to make him a mascot for successful *beurs*—French slang for people, such as the footballer Zinedine Zidane, of North African descent. He is, however, making his own political use of technology, bringing together 1,000 French business people and activists in an invitation-only online think-tank called Digital Catalyst. “There's a lot of people like me in France, but we don't know each other,” he says of the group. “It's key that the right people meet one another. If this works, we could have Politics 2.0.”

The €64m question

It may be popular with the politicians, but will Netvibes prove to be a viable business? Mr Krim has replicated the Silicon Valley start-up model right down to the “build it and they will come” attitude of the late 1990s. Rather than cluttering up users' dashboards with advertising, the obvious source of revenue, Netvibes follows a sponsorship model. *Les Echos*, for example, a business newspaper, offers a Netvibes module that provides financial alerts and drives traffic to its website. Netvibes also has revenue-sharing agreements with firms such as eBay and Snap.com that offer services through its site, but these are not yet making much money. Investors do not seem to be worried, however. A site that millions of people are using as their internet home page “will have many interesting revenue opportunities,” insists Neil Rimer of Index Ventures.

Today's trend is for start-ups to attract a large audience and then sell themselves to a giant such as Google, Yahoo! or eBay. Mr Krim's co-chief executive at Netvibes, Pierre Chappaz, did just that, selling Kelkoo (a comparison-shopping site) to Yahoo! for $575m in 2004. As the leader in personalised home pages—its MyYahoo! service has over 50m users, though it is less sophisticated than Netvibes—Yahoo! would be an obvious buyer. But Mr Krim insists that he wants to stay independent for the time being. “Since I was a little kid, I wanted to be my own boss,” he says. In a country where most students say they dream of growing up to become civil servants, this makes him—whatever Mr Sarkozy would wish—the French exception.

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India's economy

India on fire

Feb 1st 2007 | DELHI
From The Economist print edition

Corbis

India's growth rate is close to China's; but signs of overheating suggest that this pace cannot be sustained

Get article background

THE economy is sizzling and foreign businessmen and investors are swarming to Bangalore and Mumbai to grab a piece of the action. India's year-on-year growth rate could well hit double figures at some point in 2007, and the country may even grow faster than China for at least one quarter. But things are so hot there is a big problem: India's current pace of expansion may not be sustainable.

On the face of it, the figures are compelling. India's real GDP grew by 9.2% in the year to last September (the latest numbers available). Over the past four years it has clocked up an average annual pace of more than 8%, compared with around 6% in the 1980s and 1990s—and a measly 3.5% during the three decades before 1980, when highly interventionist policies shackled the economy (see chart 1). India seems to be reaping the rewards of reforms that were made in the early 1990s. These massively lowered barriers to trade and liberalised capital markets. As a result, total trade in goods and services has leapt to 45% of GDP, from 17% in 1990.

Economic growth is likely to remain strong this year, driven by booming investment and consumption. The government's five-year plan to 2011-12 has an ambitious target of 9% average annual growth. Most Indian economists expect at least 8% over the next five years. Some, such as Surjit Bhalla, of Oxus Investments, think even 10% is feasible, thanks to a surge in investment.

Optimism is abundant. Indian businessmen were the most upbeat among 32 countries surveyed recently by Grant Thornton, a London-based accounting firm: 97% of the respondents were bullish about the future. Indians are rightly proud of the huge global success of firms such as Infosys, or of Tata Steel's £5.8 billion ($11.3 billion) acquisition of Britain's Corus this week. They point to new mobile-phone subscriptions, which are running at a higher monthly rate than in China, as evidence of their economy's vigour and modernity. But look again. Perhaps the only thing really growing faster in India than China is hype.

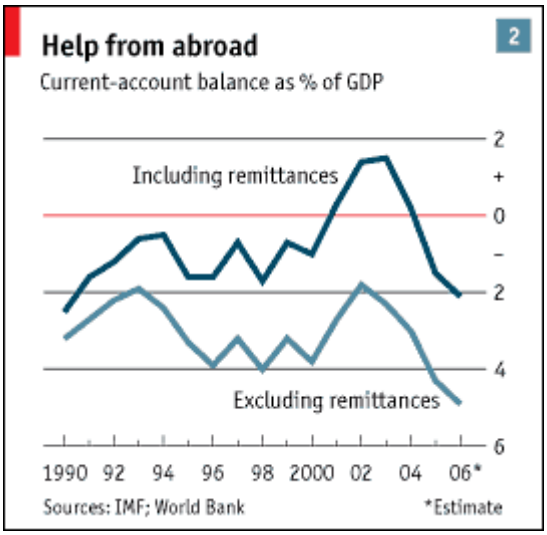
Recent visitors to Delhi were greeted by a poster campaign by the *Times of India* announcing "India poised". But poised for what? The economy is displaying alarming symptoms of overheating. This implies that demand is outpacing supply and hence the pace of growth is unsustainable. Despite lower oil prices, wholesale-price inflation has risen to 6%, which is above the 5.5% upper limit set by the Reserve Bank of India (RBI). India does not have a single rate of consumer-price inflation, but the crude average of the rates for industrial, non-manual and agricultural workers is above 7%. Capacity utilisation is higher than at any time in the

past decade and severe skill shortages have caused wages to rocket.

The RBI is also concerned about a credit boom. Bank lending to firms and households has expanded by 30% over the past year. Lending on commercial property is up by 84% and home mortgages by 32%. Asset prices look bubbly. After rising more than fourfold over the past four years, India's stockmarket is one of the emerging world's most expensive, with a price-earnings ratio of more than 20. House prices in many big cities have more than doubled over the past two years.

Against this sweltering background, the RBI's interest-rate decision on January 31st looked timid. It raised its overnight lending rate by a quarter-point to 7.5%, but left the reverse repo rate (which it uses to drain excess liquidity from the banking system) unchanged at 6%. Over the past couple of years interest rates have risen by less than the rate of inflation, so they have fallen in real terms.

The inflation numbers probably understate the degree of overheating. When demand outpaces supply in an open economy it is more likely to show up in a current-account deficit than in inflation. India's deficit widened to more than 3% of GDP in the three months to September—a huge swing from a surplus of almost 4% in the first half of 2004. And the true gap between domestic demand and supply is even bigger. Yaga Venugopal Reddy, the RBI'S governor, recently drew attention to how India's current-account deficit is larger once you exclude the money sent home by Indians abroad. These remittances do not reflect domestic demand or supply, but are more like a capital inflow. Excluding workers' remittances, India's deficit is running close to 5% of GDP (see chart 2)—larger than the equivalent deficit during India's balance-of-payments crisis in the early 1990s.



Keeping up with demand

The risk of a financial crisis is slight, because India has the cushion of $180 billion of foreign-exchange reserves, which is equivalent to 11 months' imports, and its external debt is small. But this misses the point. The reason for concern about India's widening current-account deficit is not that it heralds a financial crisis, but that it is a signal of how supply cannot keep pace with red-hot demand.

Furthermore, unlike China and most other Asian emerging economies, India is heavily dependent on short-term portfolio capital inflows, rather than foreign direct investment, which is longer-term. Short-term capital has accounted for four-fifths of capital inflows into India over the past three-and-a-half years—although, encouragingly, foreign direct investment did pick up strongly last year. This means India is vulnerable to rising interest rates if there is a sharp reversal in the appetite for risk in global financial markets.

How fast can India grow? Most standard methods of estimating the trend—or potential—rate of growth (the maximum at which an economy can expand without triggering a rise in inflation) arrive at figures of around 7%. But business people, investors and an unusually large number of economists, are convinced that India is undergoing a “paradigm shift” and so backward-looking historical data are now irrelevant for assessing future growth.

India's capacity for growth has certainly increased over the past decade, thanks to earlier reforms. Yet given widespread signs that India is already exceeding its speed limit, there is a high risk that if the economy continues to grow at 9% or more, it will get ever hotter. Inflation will climb higher and financial imbalances will widen, running the risk of a hard landing. India has no genuinely independent central bank to put on the brakes. And policymakers are understandably reluctant to cool demand when India needs rapid growth to create jobs and reduce poverty.

An alternative to slowing demand is to boost supply by speeding up reforms and attacking the many bottlenecks caused by inadequate infrastructure, dreadful public services, skill shortages and rigid labour laws. But improving infrastructure and education not only takes time, it also requires money, and India's fiscal finances are far from healthy.

On the surface, the government has made great strides to cut its budget deficit. The IMF forecasts the deficit for central and state governments will fall to 6.2% of GDP in the fiscal year ending in March, slightly below budget and down from a peak of 10% in 2001-02. Some of the reduction is due to greater fiscal prudence and reduced tax evasion, but it also reflects a cyclical upswing in tax revenue on the back of the economic boom and low interest rates, thanks to the global liquidity glut. If interest rates rose because foreign investors lost their appetite for risk, or if the economy slowed, the budget deficit would widen.

It already looms dangerously large. Chetan Ahya, Morgan Stanley's economist in Mumbai, calculates that off-budget items, such as oil and power subsidies, amount to another 1.8% of GDP. This puts the total deficit closer to 8% of GDP, the biggest among the main emerging economies. India also has the highest ratio of public debt to GDP, at 80% (see chart 3).

The budget deficit could swell further over the next few years. Generous tax exemptions for exporters in special economic zones may erode future revenues. And the government's Sixth Pay Commission, due to report by April 2008, is likely to lead to a big rise in public-sector pay. Its predecessor's report marked the start of a sharp downturn in public finances; and the new recommendations will be implemented in 2009, an election year.

Again, the concern is not that India's public borrowing causes a financial crisis. Most of it is funded through domestic, not foreign, debt and controls on capital outflows ensure that domestic savers buy government bonds. The real problem is that India's weak fiscal position constrains its future growth by leaving no room for more public spending on infrastructure, education and health.

Leaving the farm

The growth optimists point to India's favourable demography. The population of working age will continue to rise for several decades, whereas in China it is expected to fall. This, it is argued, will boost India's workforce and both saving and investment. Furthermore, 60% of India's labour force is engaged in low productivity farming. As workers shift from agriculture to more productive jobs in industry and services, this will automatically boost GDP growth. Yet this assumes the newcomers will all find jobs. If those jobs do not appear, the so-called demographic dividend will more likely turn into a demographic disaster. Some 60% of the demographic bulge will come in five poor and badly governed states.

This is just one example of how economic commentators tend to confuse India's long-term potential (what is feasible provided the best policies are put in place) with its current potential (ie, non inflationary) growth rate. That India has huge long-term potential is undeniable, but without reforms the country cannot fully exploit it.

All agree that the biggest obstacle to growth of 9% or more is India's infrastructure—especially its lousy roads, ports and power. According to the World Bank, the average manufacturing firm loses 8% of sales each year from power cuts. India spends 4% of its GDP on infrastructure investment, compared with China's 9%. In absolute dollar terms, China spends seven times as much on its infrastructure.

India's government has ambitious plans to increase total infrastructure spending to 8% of GDP over the next five years. This will involve some increase in government spending, but the idea is for the bulk of it to be financed by public-private partnerships. That will be hard.

Private investors, especially foreign ones, still shy away from sectors like electricity and roads because they are uncertain of earning a reasonable return. Only about half of all electricity generated is paid for, because power is stolen and bills are left unpaid. Saumitra Chaudhuri, the economic adviser at ICRA, a credit-rating agency, argues that public-private partnerships first require regulatory reforms to protect the interests of both investors and consumers. As the World Bank put it in a report last year, “when systems are failing, it is not enough to fix the pipes, one needs to fix the institutions that fix the pipes.”

Another obstacle to growth in manufacturing is India's labour laws, which are among the most restrictive in the world. Firms employing more than 100 people cannot fire workers without government permission, which discourages expansion. Today's central government cannot scrap these laws because it relies on the support of the communist parties. In theory, the state governments can apply the laws more flexibly, especially in the special economic zones, but this is unlikely to lead to more flexible labour markets overnight.

A third big problem is the dreadful quality of public services, from education and health to the provision of water. Half of urban households lack drinking water within the home; one quarter have no access to a toilet, either public or private. Many public services in cities have worsened in recent years. In Bangalore water is now available for less than three hours a day, compared with 20 hours in the early 1980s. This may be another reason why workers are not moving in from rural areas as rapidly as in China.

Nor are young Indians equipped for more productive jobs in the towns. The quality of education and health care is dire. A survey in 2003 found that only half of paid teachers were actually teaching during school hours. Another survey found that government health centres in poor parts of Delhi had a more than 50% chance of prescribing a harmful therapy for common ailments.

Bizarrely, India has one of the most privatised health systems in the world. Government spending accounts for only 21% of total health spending. Likewise, in eight of 18 states studied more than half of all children in urban areas are in private schools. But this is not a model for free-market economics or the result of policy reform. People go private only because public services are so bad. Subir Gokarn, an economist at CRISIL, another credit-rating agency, worries that because the educated middle class do not use public services, there is less public outcry for reform than there should be.

Sadly, the prospects for dramatic change in the near future look slim. With a few exceptions, such as the partial opening of retailing to foreign investment and the privatisation of the two biggest airports, reforms have stalled since the government took office in 2004. Despite the reformist instincts of Manmohan Singh, the prime minister, the need

to maintain the coalition overwhelms the appeal of reform.

Back to school

The supply-side constraints of infrastructure, labour laws and public services seem formidable, yet the vast majority of local economists in Delhi reckon that annual growth of at least 8% is sustainable even without further reform (with reform they look forward to 9% or more). A popular argument is that other Asian economies grew by 8-9% for long periods, so why not India? But East Asian economies invested much more in education and infrastructure than India does today.

A recent study from Goldman Sachs, which forecast that India could sustain 8% growth until 2020, was widely trumpeted in Indian newspapers. However, the bank's report clearly stated that this would require better education, labour market reforms and less red tape. Oddly, most newspapers failed to mention that.

Indeed, it is possible to detect a belief among some that it is now India's “right” to match China's growth rate of 10%. Even the finance minister, Palaniappan Chidambaram, has felt the need to remind people that present rates of growth are not “because some kind god smiled at us”. No country “deserves” rapid growth, unless it puts in place the right policies. The biggest danger of today's rampant economic optimism is that it could breed complacency about the need for reforms. That would be a sure recipe for a future slowdown.

India needs faster growth to create more jobs for its expanding population and to make it easier to relieve poverty. The awkward truth is that although the economy is sprinting ahead, most people are only crawling. Although the educated middle class has enjoyed big salary increases and a surge in the value of their homes and shares, the 60% of the population close to or below the poverty line have not yet seen a material gain.

Measured by the commonly used gini coefficient, India has less income inequality than China or America. But it has much more poverty. Some 260m people still live on the equivalent of less than $1 a day. Half of all children under five are malnourished. India needs rapid growth. But by itself that is not sufficient to end poverty, warns Rajiv Kumar, the director of ICRIER, an economic research institute. Better infrastructure and education are needed to make the rural poor more mobile so they have an escape route. In this way, better infrastructure and improved public services can not only increase growth, but also spread the rewards.

To boost sustainable growth, India needs to clear the path ahead rather than risk running an economy beyond its safe maximum speed. Indians are understandably eager for their economy to sprint like a tiger rather than amble along like an elephant. Yet few animals have an elephant's stamina or can travel as far in a day—provided its way is not blocked.

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Financial stability

What keeps bankers awake at night?

Feb 1st 2007
From The Economist print edition

Satoshi Kambayashi

The more people worry about risks within the financial system, the better

WHEN the great, the good and the media assembled in Davos for the World Economic Forum in January, one topic dominated the financial agenda—risk. That ought to be a good sign. For it is when those in charge are feeling complacent that disaster is most likely to happen. Investors also seem nervous. A survey of fund managers by Merrill Lynch, an investment bank, found 82% expected volatility to rise this year.

However, as the Bible says, “by their fruits ye shall know them”. Banks are still financing leveraged buy-outs, junk bonds are offering their lowest spreads since March 2005, and the cost of insuring against a share-price fall, as measured by the Chicago Board Options Exchange Volatility Index (Vix), is low (see chart below). Financiers may be worrying about risk, but they do not seem to be doing much about it.

That apparent dichotomy reflects a broader debate. Some argue that the “great moderation” in economic numbers such as inflation and GDP growth has reduced risk for investors. Furthermore, the greater sophistication of financial markets has improved the pricing and the distribution of risk. Recent tests of the system, such as the collapse of Amaranth Advisors, a hedge fund, last year, have proved its resilience.

Sceptics retort that the calm of markets is an illusion caused by benign economic conditions and excess liquidity. The greater dispersion of risk means nobody knows where it is. And as Warren Buffett, the billionaire investor, has remarked, “It's only when the tide goes out that you learn who's been swimming naked.”

Into these choppy waters has stepped Britain's regulator, the Financial Services Authority (FSA). Its latest *Financial Risk Outlook,* an annual exercise, is a study in defensive drafting. You should be reassured that: “the risk of a financial stability event occurring is relatively remote...” But not too reassured, as the FSA goes on to say “...although there is a range of plausible event risks that could crystallise.”

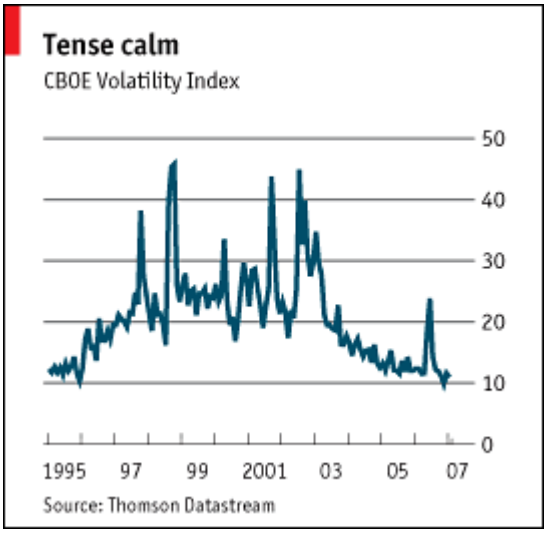
More useful are the FSA's “alternative scenarios” about what could threaten the stability of the system, including a flu pandemic, a deterioration in personal-credit quality, and (somewhat tautologically) a reappraisal of risk by investors. The regulator worries that financial companies “underestimate the likelihood of severe events or, where mitigating action is envisaged, they overestimate their ability to take action that is both effective and timely.”

It is the job of regulators to worry, but if anything, the FSA sounds more sanguine than some of its international counterparts. Jean-Claude Trichet, the president of the European Central Bank, said at Davos that investors needed to prepare for a repricing of assets because of potentially unstable conditions. “We don't know fully where the risks are located,” he added.

This lack of information is indeed one of the regulators' main problems. A generation ago, risk was concentrated in the banking industry. That was good in one way, since regulators could monitor the banks' lending and impose

reserve requirements. But when a bank failed, the effects were widespread because of the impact on depositors and other banks.

Nowadays, the banks have parcelled out the risk to hedge funds, pension funds and insurers. But has risk gone out the front door, only to come in the back, because of the banks' trading and financial relations with those same counterparties?



Information is also constrained by the off-market nature of many of these transactions. Many derivatives are traded “over the counter” rather than on a public exchange; companies are deserting stock exchanges for the arms of private-equity groups; new issues of bonds and equities are increasingly made via private placements rather than public offerings. This makes it hard for regulators to discern how markets would react in a crisis, especially since there has not been a severe global recession since the early 1990s.

Two things worry people. The first is the “carry trade”, which involves investors borrowing a low-yielding asset (often the yen) and buying a higher-yielding one. Past financial-market wobbles have been associated with periods when the carry trade was unwound. No one knows precisely how much capital is involved. But Tim Lee, of Pi Economics, reckons as much as $1 trillion may be staked on the yen carry trade. Were the yen ever to rise sharply (making the trade unprofitable), there could be hell to pay in the markets.

The second is the low cost of credit, and the rapid growth in credit derivatives, which allow investors to insure against default. The rise of the derivatives market has coincided with a very low default rate. Were defaults to rise, the ability of the markets to absorb losses (and clear trades) might be severely tested.

At least these risks can be observed. Until they can be quantified, it makes sense, as the FSA suggests, for finance firms to ensure their paperwork is in order, and to stress test their systems while conditions are benign. The worst time to call a plumber is in the middle of a freeze. And perhaps investors are more aware of risk than you might think. Although the February 2007 Vix contract is low, those who want to protect against volatility until May 2008 have to pay a 40% premium. So not everyone is complacent.

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Buttonwood

Crude suggestion

Feb 1st 2007
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There may be an ominous link between oil and bond prices

WHEN stockmarkets fall precipitately, the story makes the nightly television news bulletins. But sudden moves in bond prices rarely attract anything like as much attention, even though the fixed-income market plays a vital economic role, setting the borrowing rate for governments, companies and homeowners.

So people can be excused for not noticing the recent tumble in American bond prices, which had driven yields sharply higher before a slight recovery on January 31st. On that day, the ten-year Treasury bond was yielding 4.83%, almost half a percentage point above its level at the beginning of December (see chart). The 30-year yield, until a decade ago the world's benchmark, was close to 5%.

The obvious cause for the change in mood is the American economy and the policy stance of the Federal Reserve. At the start of December most people thought the Fed would cut interest rates in the first half of 2007, in response to an economic slowdown. But recent data have been stronger than expected, causing most economists to push back their expectations of rate cuts.

However, the bond market is a lot more complex than you might think from the simple mantra of “rate rises bad, rate cuts good”. For a start, bonds can operate as a kind of negative-feedback system; when yields rise, so do mortgage rates (particularly in America, where loan rates are linked to bond yields). Higher rates damage the housing market, and thus the broader economy, a development that can send bond yields back down.

Then there is the complex relation between bonds and oil prices. In the 1970s higher crude prices simply meant rising inflation, which was bad for bonds. Nowadays, thanks in part to sounder monetary stewardship, the relationship has reversed; higher oil prices mean a weaker economy, which is good for bonds.

The oil-bond nexus has acted as a thermostat for the global economy. Higher crude prices restrict demand, cooling the economy down. But the resulting lower bond yields then boost consumer confidence, heating the economy up again. And, as in recent months, falling oil prices (good for consumers) have been accompanied by rising bond yields (bad).

The linkage goes further. When oil prices rise, money flows into the coffers of the producers. Some believe this has helped push bond yields down, because the petrodollars are invested in American Treasuries, much as Asian countries invest their surplus savings.

But pinning down a direct correlation is tricky. Barclays Capital points to a clear connection between oil prices and holdings of Treasury bonds by the Organisation of the Petroleum Exporting Countries (OPEC). But an IMF study* has found few links between oil prices and ten-year Treasury yields, and a paper** by Raman Toloui of PIMCO, the fund management group, suggests an indirect relationship at best. He shows how oil exporters have recently been amassing reserves faster than Asian governments have—last year, he estimates that they generated some $500 billion of reserves, against $284 billion in Asia. Much of this surplus ends up in central banks, or in government outfits like the Kuwait Investment Authority. Mr Toloui reckons that every $10 rise in the price of crude brings oil exporters an extra $90 billion-100 billion a year. Their assets add up to at least $1.5 trillion.

It is not possible to get accurate data on where all this money has been invested. But Mr Toloui reckons that some 40% can be pinned down. The vast bulk (two-thirds) is invested in bank deposits and short-term securities. Only 3% is put into long-dated American Treasuries.

So that would not, at first sight, seem to suggest that oil money has been driving bond yields up and down. Consequently, there should be little reason to fear that lower oil prices will remove a big buyer from the Treasury-bond market.

However, it may be that oil money flows into Treasuries via an indirect route, for example through fund managers acting on the oil nations' behalf. And even if an OPEC country invests its reserves in, say, Japan, that only gives the Japanese more money with which to finance the American current-account deficit.

Americans may, therefore, have just cause for some concern about their bond markets. The oil exporters do not appear to be as keen to buy dollars as do Asian central banks—which want to control their exchange rates to ensure their exports remain competitive. And even Asian nations, such as China, are talking about finding new ways of investing reserves.

In the long run, this could mean that Americans would have to pay more to finance their current-account deficit—a bearish sign. The recent rise in bond yields could be a first step in that reckoning.

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*"The Impact of Petrodollars on US and Emerging Market Bond Yields", IMF, April 2006.

** "Petrodollars, Asset Prices and the Global Financial System", PIMCO.

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The IMF

Funding the fund

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From The Economist print edition

Putting the IMF's own house in order

THE financial missionaries of the IMF unpack their suitcases in some of the finest hotels in the world, but their offices in Washington, DC, are in need of refurbishment. An overhaul of the fund's fittings and fixtures was stopped halfway recently, leaving its interior stuck between the 1970s and a sleeker, modern era.

This is just one sign of the IMF's straitened circumstances. This fiscal year it must endure a freeze, in real terms, in its $980m budget for staff, travel and other administrative costs. By 2010 it projects a budget shortfall of about $370m a year. Last May the fund's managing director, Rodrigo de Rato, invited eight “eminent persons”, led by Andrew Crockett, former head of the Bank of International Settlements, to dream up new ways to fund the fund. On January 31st they offered their answers.

Mr Crockett started by noting the perversity of the way the IMF pays for itself. “The fund does well when the world economy does badly,” he said, which creates a “curious incentive structure.” It is the mirror image of the unseaworthy economies it used to bail out. In the stormy period from 1994 to 2002, the fund repeatedly called on the “quotas” of hard currency pledged to it by its big shareholders to make large loans to troubled economies. Since it charged its borrowers more than it paid its creditors, it could afford a big expansion of its operations. The fund's retinue of economists, managers and other professionals grew from 1,488 in 1997 to 1,999 in 2005. Its administration costs more than doubled.

But the fund's interest earnings are drying up as it struggles to find new takers for its money. Instead of relying on the fund, emerging economies are insuring themselves by amassing reserves of their own. Some, such as Brazil, Argentina and Indonesia, have paid off their IMF loans early, at a cost, to rid themselves of its “stench”, as some people put it. Now, a loan to Ankara accounts for two-thirds of its credit outstanding: the IMF is, in effect, the Turkish Monetary Fund.

What should the new TMF do? Mr Crockett's committee thinks three fingers will more or less suffice to plug the dyke. First, the fund has squirreled away almost $9 billion of reserves, set aside when business was booming. It should invest these reserves “slightly less conservatively”, Mr Crockett says, thereby raising an extra $45m a year. Second, instead of waiting for a crisis before tapping the hard-currency quotas promised by member governments, it should dip into them as a matter of course, investing the proceeds in safe securities and creaming off a slice of the returns for itself. If it invested $30 billion of its quotas, it could raise another $300m.

The third proposal is likely to be the most controversial. The IMF has long sat on a pot of gold: 3,217 tonnes of it, the third-biggest official hoard in the world. Mr Crockett thinks it should sell about 400 tonnes, which would raise about $6.6 billion. This would not disturb the gold market, he says, as long as central banks agree to cut their own bullion sales. With the money it raises, the fund could set up an endowment and live off the income, envisaged at $195m a year in real terms.

The fund cannot sell its gold without a vote of approval from an 85% majority of its board. America thus holds a veto, and its Congress may not be sympathetic to such schemes. Governments gave gold to the fund in the first place to underpin its lending, not to pay its salaries. If it no longer needs the bullion, perhaps it should repatriate some to its members. And if it needs money for an endowment, it should ask for one directly: as a gift from its members, accounted for in their budgets.

Like its interior decor, the fund now straddles two eras, unsure which is future and which past. If no more than a handful of emerging economies ever need or trust it again—a distinct possibility—it would either have to close its doors or find a new role, as well as a fresh pot of money. Mr de Rato entertains visions of his institution becoming what one might call an International Monetary Forum, helping to resolve global imbalances and police misaligned exchange rates through the sheer force of its analysis and argument. The staff? Well, many of them seem rather attached to their old furniture.

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Internet banking

Bricks 'n' clicks

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Citigroup gets to work on an Egg

"IF YOUR bank could start over, this is what it would be." So went the tagline of WingspanBank.com, the internet-only outfit launched by Bank One (now part of JPMorgan Chase) in 1999. But rather than revolutionising banking, it folded its cyber-wings within two years, not long after Citigroup pulled the plug on Citi f/i, its own online venture.

Now Citi is at it again. Its decision on January 29th to buy Egg, a struggling internet bank owned by Prudential, a British insurer, puts another nail in the coffin of standalone internet banking. The deal, worth £575m ($1.13 billion), gives Citi 3m credit-card customers in Britain and a low-cost way to gather deposits in a country crammed with branches. It also underlines the growing attraction of "bricks 'n' clicks" banking. Since Citi launched CitiDirect, its new online bank, in May it has gathered over $11 billion in deposits, the equivalent of opening 150 branches.

Attracting cash online does not come cheap. Citi pays 4.75% for internet deposits, multiples of what it pays for holding deposits at a branch. HSBC, a British bank, is paying as much as 6% to its online customers. Competition from mortgage, credit-card and insurance banks such as Washington Mutual, Capital One and Allstate Bank, means rates are likely to remain high. But high rates may still be cheaper than building and staffing branches.

According to Celent, a research firm, online core deposits (those with balances under $100,000) of $162 billion in 2006 are still less than 4% of core deposits across America. But the amount is expected to swell to $377 billion by 2010. Sanford Bernstein, an investment bank, says internet clients provided over a tenth of new deposit growth in the past year; they could account for over half the growth in four year's time.

The most successful standalone holdout is ING Direct, one of the pioneers. The subsidiary of the Dutch bank has attracted $60 billion in deposits by offering online savings accounts with no fees, no minimum balances and high interest rates. In America its on-the-ground presence is limited to a handful of sleek, neon-orange cyber-cafes offering free internet access and tolerable coffee.

But Bruno Paulson, of Sanford Bernstein, says the hybrid banks with internet offerings are already making life uncomfortable for exclusively online banks by generating higher returns. He says ING Direct invests most of its deposits in high-quality—and thus low-yielding—securities, providing it with a relatively skimpy 12% return on equity. It is building an online mortgage business to find more lucrative uses for its cash, but may struggle to compete with those that already peddle mortgages, credit cards and business loans through their branches.

Yet hybrid banks have their own headaches. One is cannibalisation; about a fifth of CitiDirect's deposits, for instance, have come from its own branch customers. Another is knowing when to sacrifice branches. Washington Mutual recently announced it would close 4% of its branches—in part because of its success in gathering deposits on the internet. Citi, whose branch network is surprisingly slim for the world's biggest bank, may have less cause for concern.

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Stock exchanges

Flying in formation

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From The Economist print edition

Bourses, like airlines, may benefit from global alliances

FOR the dwindling number of souls who cling to a vision of a single, global financial exchange, this week must have given pause for thought. Two events—an alliance between the New York Stock Exchange (NYSE) and Tokyo Stock Exchange (TSE), and the failure of America's Nasdaq to buy the London Stock Exchange (LSE)—offer reminders of the hurdles to the cross-border consolidation of exchanges.

Instead, at least in the near-term, exchange operators are likely to act as partners building up flexible global networks, rather than predators. In so doing they might look to the airline industry where a handful of alliances provide global coverage, while enabling individual members (many of them national flag carriers) to retain their independence. In a compromise between chauvinism and scale economies, users gain greater choice and flexibility as well as shared technology, without offending national regulation and political resistance to foreign ownership. Similar forces are at work in the exchange world.

It is the NYSE—the world's biggest stockmarket and, until recently, one of the more resistant to change—that is suddenly most keen to be seen building a global team. Even though it has not yet digested Euronext, a pan-European exchange operator it has agreed to acquire, the NYSE is sewing up smaller deals farther afield. On January 31st it announced plans to co-operate with Tokyo in areas ranging from technology to product development. The NYSE already lists 19 Japanese companies and hopes for more. But until the TSE goes public, possibly in 2009, its options for more formal tie-ups are limited; without common ownership, it remains to be seen how users will benefit from the new alliance. A few weeks before, the NYSE signed an even more significant deal in Asia, when it led a group of investors who bought a 20% stake in India's National Stock Exchange. John Thain, boss of the NYSE, says he is looking for more deals around the world.

Such an alliance model is on display elsewhere, too. In the derivatives world, the Chicago Mercantile Exchange has successfully attracted both the Chicago Board of Trade (which it is buying) and the New York Mercantile Exchange on to its Globex trading platform, making the “Globex alliance” a powerhouse in international futures trading. And in central Europe, a cluster of stock exchanges co-operate in areas such as product development.

The LSE's spirited rejection of its latest foreign suitor was hardly a shock, and illustrates how hard it is for an overseas rival to take over a national icon. The London exchange has fended off a barrage of potential acquirers in recent years, a tactic tacitly supported by British authorities eager to shield it from foreign regulation. Meanwhile, Nasdaq's hopes of keeping pace with its New York rival on the world stage look more forlorn than ever. In future, the NYSE may even try to grab the London exchange for itself.

Mr Thain hopes that the globalisation of markets will push regulators to harmonise their stock-exchange rules, making real consolidation easier. Already, the flurry of transatlantic bids has encouraged American and British regulators to co-operate more closely. But few are holding their breath for anything deeper anytime soon. Financial exchanges come with a lot of political, cultural and emotional baggage. This is a shame: consolidation can offer many benefits. Until the baggage is set aside, though, alliances may offer the best alternative to acquisitions. Their success should be measured not only in returns to shareholders, but also in benefits to customers. The airlines have done it—the exchanges can too.

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China Life

Take cover

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Investors—and clients—have flocked to the largest Chinese insurer

TO CONFORM to the rules of the Shanghai Stock Exchange, China Life announced on January 30th that its reported earnings in 2006 would be up by more than 50%. Its shares promptly fell 2%. One reason for the raspberry may have been that investors thought a 50% earnings increase was a comedown, given China Life's recent performance (though when full results come out in April, they will probably be up by even more). Another explanation is that Chinese investors are at last questioning the stockmarket's euphoria; its index fell almost 5% on January 31st.

China Life is perhaps the most vivid example of the torrid state of China's domestic share prices. A simultaneous public offering in New York and Hong Kong in 2003 was a bit of a dud; by mid-2004 the shares were below the offer price, but they began to rise in 2005 and in 2006 they quadrupled. Between late December and early January, the insurer's value fell almost 15% in Hong Kong and New York, but “A” shares issued on January 9th in Shanghai to Chinese investors quickly doubled. Now China Life's market value is around $130 billion, second in the world only to American International Group (AIG), which, along with other foreign-run insurers, was thrown out of China as a result of the Communist revolution.

The measures used to value China Life suggest, to put it mildly, that something unusual is going on. Ordinarily, life insurers are valued at about twice their book value. China Life's shares trade for eight times book, or more, depending on the share class used.

The enthusiasm is not without reason. China Life is the undisputed heavyweight in the fastest-growing big market for insurance, with 45% of the life business and similar dominance of accident and health insurance. Its clients' assets under management exceed those of China's mutual-fund industry. With 640,000 agents and outlets in 90,000 banks, no firm can match its sales force. At the time of the Hong Kong offering, it had 44m policies in force; now it has 70m, and because of China's expanding wealth and fraying public safety nets, excellent opportunities for growth.

But some frailties are emerging. Premium growth is slowing, reckons Citigroup in a report. And competition is coming. There are now 45 insurance companies in the market, up from eight a decade ago. But at the moment, its position looks secure. Its most popular offerings are investment products with an insurance wrapper, life insurance providing a guaranteed rate of return a bit over 2%, and, in many cases, the prospect of a dividend tied to investment results. That is a better deal than the low rates offered on deposits by the country's banks. There are not many other legitimate options for savings—other than paying bubble-like prices for shares on the Shanghai exchange.

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The Federal Reserve's Chairman

Hitting his stride

Feb 1st 2007 | WASHINGTON, DC
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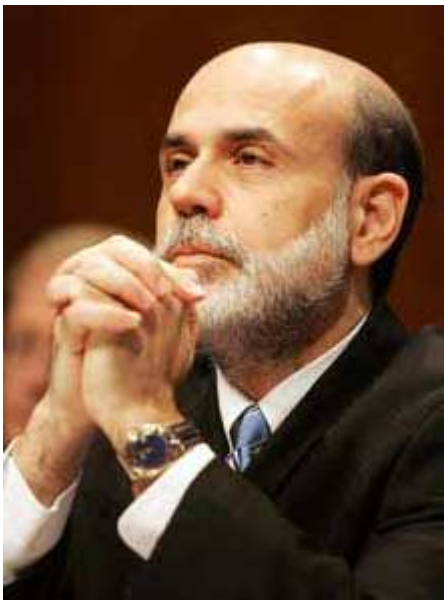
Ben Bernanke has won respect. Will he now push reform at the Fed?

AFP



A year older, a year wiser

WHEN Ben Bernanke succeeded Alan Greenspan as chairman of America's Federal Reserve a year ago this week, Wall Street's commentariat had two questions. Would “Helicopter Ben” prove to be a credible inflation fighter? Many bond traders remembered him as the Fed governor who had once mused about preventing deflation by dropping money from the sky. And at what pace would the former Princeton professor push the Fed towards adopting a formal inflation target, an idea he had long championed? One year on, the answers seem to be “yes” and “slow”.

After a rocky start, Mr Bernanke has won inflation-fighting credentials (see chart below). Last May was a low point. The new Fed chairman told congressmen that the central bank might pause its interest-rate increases even if inflation was rising. Bond markets took this to mean that a pause was imminent and inflation hawks began to fret. He compounded the mess by confiding to a journalist that the markets had misinterpreted him.

Though serious, that setback proved short-lived and the chairman's reputation has steadily risen since last summer. That is largely because his judgments have proved correct: notably, to stop tightening in August with rates at 5.25% yet retain a hawkish bias despite the housing recession. Inflationary pressure has abated and, as Mr Bernanke argued, the economy has seemed to shrug off the housing market.

Two months ago financial markets were sure that the Fed, for all its hawkish talk, would soon cut rates. But as the statistics have strengthened, Wall Street has fallen into line with Mr Bernanke. Far from heading for recession, preliminary figures released on January 31st showed output rose at an annual rate of 3.5% in the last three months of 2006, above the economy's trend pace. On the same day, the Federal Open Market Committee (FOMC), the central bank's policymaking body, said it was once again holding rates at 5.25%. Although it acknowledged that inflation figures have improved “modestly”, it kept its hawkish bias.

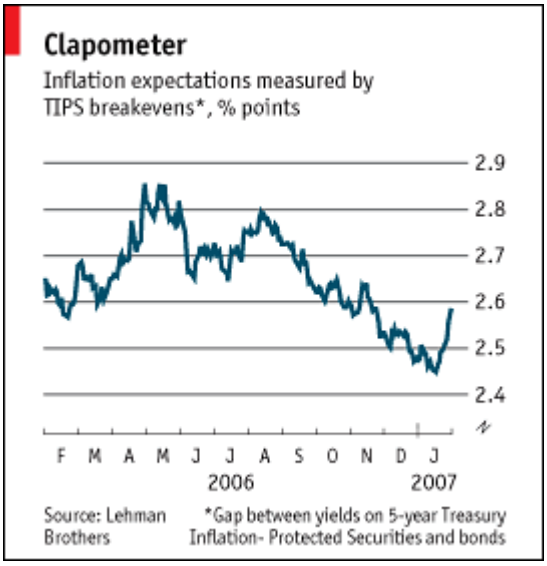
Meanwhile, Wall Street is gradually getting used to the style of the Bernanke Fed, which seems to be more democratic than the Greenspan model. Mr Bernanke has altered the format of the FOMC's discussions to encourage debate. Don Kohn, the Fed's vice-chairman, is particularly influential: he gave the speech that has had the biggest impact on the markets in the past six months. Dissent is tolerated: Jeff Lacker, president of the Federal Reserve Bank of Richmond, disagreed with the decision to halt tightening in August and dissented at every subsequent FOMC meeting until his stint as a voting member ended in December.

This collegial approach is one reason why the Fed has moved more slowly towards inflation targeting than many outsiders expected. Although several governors agree that such a target makes sense in principle, they are loth to change a system that seems to be working well. Mr Kohn, a sceptic, is in charge of a special committee to guide the deliberations. It seems in no hurry. Nor are the external circumstances auspicious. With the Fed's preferred price gauge, the deflator for personal consumption expenditures excluding oil and food, still above the 1-2% that is widely read as an informal goal, the central bankers have not been keen on making a target explicit.

The change of control in Congress has slowed progress too. Democrats are particularly suspicious of inflation targeting, fearing it would compromise the Fed's other statutory goal, that of maximising employment. Barney Frank, the chairman of the House Financial Services Committee, has grave doubts about the idea.

Internally, rapid turnover has made matters harder. The FOMC is full of new faces. Besides Mr Bernanke, three Fed governors have arrived in the past year and one seat is still vacant. One of the newcomers, Frederic Mishkin, is a well-known advocate of inflation targeting. There is change at the regional reserve banks too. Charles Plosser, a former economics professor, became president of the Philadelphia Fed in

August. Jack Guynn retired from the Atlanta Fed in October; his successor has not yet been named. The presidents of the Boston and Chicago Feds, both voting members this year, recently said that they would be stepping down. Though they are far from agreeing to an explicit inflation target, the central bankers are discussing other ways to improve transparency. One option is to release more frequent economic forecasts. The central bank now publishes projections for growth, inflation and unemployment twice a year, based on estimates by board members and regional reserve banks. Possible changes include issuing quarterly forecasts with a more detailed description of the economic outlook. A baby step, perhaps, but in the right direction.



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Economics focus

Momentous modelling

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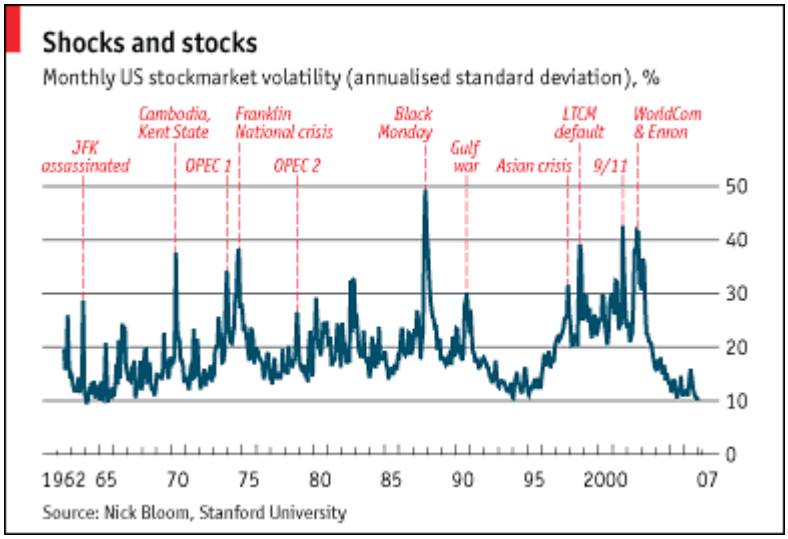

When terrorists strike, what happens to investment and jobs?

ECONOMICS is a shocking profession. No, no: it's not that economists are incompetent, work in squalor or have unsavoury personal habits. Shocking is what economists do. They start with a model of the economy, administer a "shock" to it—a sudden rise in the oil price, say, or some technological advance, or a cut in tariffs—and work out what happens to output, prices, employment and so forth. Suppose oil prices jump: output goes down, the price level goes up; depending on inflationary expectations and the response of the central bank, a persistent bout of inflation may follow. Plug in plausible numbers in the right places, using some fancy statistics and a dose of computing power, and you can estimate how big the effects might be.

Almost all these exercises deal, in effect, with changes in a number's mean or expected value (in statisticians' language, the "first moment" of its probability distribution): what if the oil price doubles? Economists have spent remarkably little time working out what will happen if the world becomes less certain: what if the oil price is likely to range between, say, $20 and $100 rather than between $50 and $60? Questions of this sort (about the "second moment") are certainly more difficult to answer—the maths is harder, for one thing—but important nonetheless.

They are important partly for the simple reason that people's behaviour may change if the world suddenly becomes a less (or more) certain place. Moreover, points out Nick Bloom, a British economist at Stanford University, events that increase uncertainty, measured by the volatility of American share prices, are fairly frequent. The most obvious recent example of a big second-moment shock is the terrorist attacks of September 11th 2001; but there have been plenty of others in the past few decades, from the assassination of John Kennedy to the collapse of Long-Term Capital Management and Enron (see chart).

Economists have not shied away from second-moment shocks altogether. Indeed, in 1983 a young American economist named Ben Bernanke published a paper* analysing how investment would be affected by uncertainty. Uncertainty, he argued, could increase the return to firms from waiting rather than making irreversible investments. Mr Bloom has revisited the subject, with the fuller treatment that modern modelling and computing tools allow. In a paper† presented at last month's annual meeting of the American Economic Association in Chicago, he builds a model in which firms choose how much to invest and how many workers to employ. The world in which they operate is uncertain, in that their revenues can vary. He introduces an "uncertainty shock" into the model by supposing that the variability of firms' revenues suddenly rises: using data from shocks over the past 45 years, he supposes that the standard deviation, a common measure of variability, doubles before returning to its old level within a few months.

Wait a moment

The model predicts, as does Mr Bernanke's, that firms wait and see what happens. Because the future is less certain,

the probability that demand will be very low (or very high) is higher. The value of waiting thus increases. Firms that would otherwise have increased investment or taken on more workers postpone their plans. Meanwhile, shrinking firms hold off sacking people, but the net effect is that investment and employment fall. Productivity also drops: because hiring and firing have been put off, workers are no longer being shuffled from less productive to more productive firms. As uncertainty returns to normal levels, investment, employment and productivity bounce back.

Mr Bloom thinks that this model fits the aftermath of the September 11th attacks reasonably well. Net employment growth in America fell sharply in the three months following the attacks—judging by forecasts made by economists in mid-August, there were 1m fewer jobs than expected by the end of the year—but rebounded in the first quarter of 2002. Investment also dipped and recovered. The perception that uncertainty increased also shows up in central banks' minutes of the time. One central banker spoke of some households and businesses entering “a wait-and-see mode...They are putting capital-spending plans on hold.”

For policymakers, says Mr Bloom, it is important to tell second-moment shocks, which seem not to last long, from the first-moment variety, where the effects endure for longer. If central bankers mistake a temporary rise in uncertainty for a permanent shock, they may, say, cut interest rates by more than they need to, with inflationary results. To make matters harder, first- and second-moment shocks are likely to come at the same time.

Mr Bloom thinks that the Federal Reserve and other central banks reacted wisely to the attacks of September 11th. Still, he suggests a couple of bits of information that may help distinguish the two types of shock. First, a spike in stockmarket volatility is a sign of increased uncertainty. Second, the different types of shock should have different effects on firms. A bad first-moment shock will reduce activity across the board. But a rise in uncertainty that causes all firms to put their plans on hold will stop (or slow) growing firms, but bolster shrinking ones.

Are uncertainty shocks always transitory? Almost. None of the examples in the chart lasted long. Looking back over the past century, Mr Bloom can point to only one such episode: the Great Depression. Between 1929 and 1932, average stockmarket volatility was 30% greater than after the 2001 attacks. A prolonged bout of uncertainty—compounded by bad policy—dampened the “animal spirits” by which John Maynard Keynes set such store, with catastrophic effects on investment and jobs. The direct macroeconomic consequences of September 11th, for all the deadly terror of that day, were much briefer.

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*“Irreversibility, Uncertainty and Cyclical Investment.” Quarterly Journal of Economics, February 1983.

†“The Impact of Uncertainty Shocks: Firm Level Estimation and a 9/11 Simulation”

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African science

Local heroes

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From The Economist print edition

Panos Pictures

Good science does get done in Africa, though it tends to go unnoticed

AFRICA is where researchers go to carry out exotic fieldwork—at least, that is a common presumption in rich countries. It is a useful place for studying elephant behaviour and discovering early hominid remains; then the scientists return home, write papers and enjoy the kudos of getting them published in oft-cited journals.

This, however, is only part of the picture. Nigeria, for instance, has about 40% of the world's sickle-cell-anaemia patients. Last July, a drug company called Xechem Nigeria started selling a new medicine for the disorder. This medicine, Nicosan, had been developed by the country's pharmaceutical research institute. And, at a more esoteric level, the Southern African Large Telescope, located in South Africa's semi-desert Karoo region, is the joint-biggest such instrument in the world.

Despite these successes, many African scientists feel neglected by their politicians who, they suspect, do not understand that geeks as well as businessmen are crucial to economic development. That, however, might be about to change. For the first time, the theme of the twice-yearly African Union Summit (held on this occasion in Addis Ababa) was science, technology and climate change. Although not everything went to plan ("I have a crisis meeting with ministers to discuss how they got beaten by soccer on the agenda," read one speaker's BlackBerry message to *The Economist*) such a high-level discussion of the role that science can play in Africa's development was long overdue.

Though the summit's conclusions were limited (many decisions were put off until a re-match next month), that Africa's politicians are taking any notice at all of their continent's science is encouraging. It is, of course, possible to free-ride on the science and technology of others. But in Africa, as elsewhere, no one knows better than the locals exactly what technology needs to be created, and no one has a greater incentive to create it. Nor need such technology be of the unsophisticated kind often badged as "appropriate" by well-meaning outsiders. Appropriate technology can be very sophisticated indeed.

Brothers in arms

The African Laser Centre, for example, is that most trendy of things, a virtual organisation. This means it can draw on talent from different countries without requiring people to move. One of its first projects is to design a laser-based gadget that can diagnose the condition of crops. For this project, the collaborators are a Ghanaian, Paul Buah-Bassuah, who works at the University of Cape Coast, and a South African, Hubertus von Bergmann, of the University of Stellenbosch.

Chlorophyll, the molecule that is at the heart of the process of photosynthesis, absorbs the short and long wavelengths of visible light (blue and red), and reflects the stuff in the middle (green). It is the absorbed wavelengths that are used for photosynthesis, so measuring the efficiency of that absorption gives an indication of a plant's health.

The device devised by Dr Buah-Bassuah and Dr von Bergmann contains a laser that produces blue light of the wavelength preferred by chlorophyll. In a healthy plant the energy from this light will, once it has been taken in by a chlorophyll molecule, be passed on to other molecules and used to make sugar. In a plant that is stressed by lack of water or nutrients, however, such a transfer of energy is harder to effect, and if the chlorophyll cannot pass its energy on, it simply re-radiates it—a process known as fluorescence.

When the laser in the device is shone onto a leaf or fruit through a fibre-optic cable, the light excites chlorophyll molecules inside the cells. Any fluorescent re-emissions travel back along the optical fibre to a detector that analyses both the amount and the nature of the fluorescence.

According to Dr von Bergmann, the amount of re-emitted light can vary by as much as 80% between a healthy and an unhealthy plant. The nature of the fluorescence is also important. The re-emitted light is not blue. Instead, it is a mixture of red and infra-red. The more infra-red light the mixture contains, the fewer functioning chlorophyll molecules there are in the leaf or fruit being examined.

Laser laboratories, virtual or otherwise, are still a rarity in Africa. The continent, however, does produce some of the world's top veterinary livestock research.

From the perspective of poor farmers, animal diseases can be placed into three categories. Some, such as Newcastle disease, for which H5N1 flu was first mistaken in Nigeria, reduce their assets by killing livestock. Others pose limits to their productivity. East Coast Fever, for instance, hits non-indigenous but meaty breeds of cattle harder than the scrawny, local zebu. That puts cattle farmers in the east and south of the continent, where the disease is endemic, on the horns of a dilemma when they choose which breeds to ranch.

It is the third category of disease, though, that is most economically devastating. This is the sort that shuts down farmers' access to their markets because the buyers are afraid of it spreading.

Rift-valley fever falls in this third category. For centuries, nomadic herders in areas now under the control of Djibouti, Eritrea, Ethiopia, Somalia and Sudan sold sheep and goats to customers across the Red Sea for sacrifice during the *haj* pilgrimage to Mecca. Until nine years ago, this trade involved millions of animals. But then, a massive outbreak of rift-valley fever led Saudi Arabia to impose a trade ban, and to buy more expensive Australian livestock instead.

Some scientists, such as Assaf Anyamba, from Kenya, are trying to tackle the problem by using satellite images to forecast how much rain will fall in various parts of the Horn of Africa. Eggs of the mosquito that transmits rift-valley fever must dry out and become wet once more if they are to develop into adults, so an accurate forecast of periodic flooding is the key to predicting where the disease will break out. That might help herders avoid those areas. But a vaccine would be better.

This is what Felicity Burt, of the University of the Free State, in Bloemfontein, South Africa, is trying to create. She has taken a virus called sindbis, which does not cause serious symptoms, and swapped the genes that code for its protein shell with a selection of those that do the same job for the rift-valley-fever virus. When her vaccine is injected into an animal, it causes the production of rift-valley viral proteins without the associated fever. The immune system can then learn to recognise those proteins, so that it can react rapidly if it encounters real rift-valley viruses.

So far, the vaccine seems to work well in mice—protecting them against infection. Whether it protects sheep has not yet been tested, although it certainly causes them to produce the appropriate antibodies. Unfortunately, that needs two inoculations, and an ideal vaccine would need only one. Nomadic herders, by definition, are rarely found in the same place twice, so tracking them down to give their animals a booster shot is difficult. One way to create a single-shot inoculation might be to insert extra or altered promoter elements–which switch genes on and off—into the sindbis virus's genetic material. That should increase the amount of rift-valley proteins made in an infected cell.

Such genetic modification is also finding a place in African crop science. Jennifer Thompson and Edward Rybicki, of the University of Cape Town, have developed a variety of maize that is resistant to maize-streak virus, another insect-borne disease (the culprits here are leaf-hoppers). Maize is not native to Africa, even though it now, for instance, occupies 90% of the cultivated land in Malawi. But since its arrival from the Americas in the early 1500s, a virus found in local grasses has evolved a way to attack it. In bad years, such as 2006, maize-streak virus can wipe out entire harvests. Plant breeders have tried for a quarter of a century to develop crops that are immune to the disease by crossing maize with partially resistant native grasses. Unfortunately, they have met little success. The pattern by which resistance genes are inherited has proved elusive.

Dr Thompson and Dr Rybicki's trick was to insert a modified viral gene into the maize. This gene encodes a mutated version of one of the proteins that the virus needs to copy itself. When expressed at high levels in a plant infected with maize-streak virus, the modified protein outcompetes the normal version, throwing a spanner into the works of viral assembly. That has been demonstrated in greenhouses, at least, by Panner Seeds, a seed supplier in Greytown, South Africa. And the trait has successfully passed itself down four generations of crop. If further crosses go well, field trials will take place later this year. Those would be the first such trials of a genetically modified crop in Africa, and if successful, this maize would be the first genetically modified crop created in a developing country—the first, it is to be hoped, of many.

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Agricultural pests

White death

Feb 1st 2007
From The Economist print edition

A diabolical pact between an insect and two viruses

THOUGH the example comes from China, the sort of problem that African agricultural researchers have to grapple with (see article) is well illustrated by a paper in this week's *Science* about the whitefly *Bemisia tabaci*—an insect that is not actually a fly, but is related to aphids and leafhoppers.

Whiteflies are pests in every continent that they are found in—and they are found in every continent except Antarctica. They cause damage directly, by consuming plant juices, and indirectly, by spreading viral diseases. But Liu Shusheng, of Zhejiang University, in Hangzhou, and his colleagues have found a strain of the species that delivers a double whammy. Not only does it spread diseases, but it is also vastly more successful when it lives on plants infected with the diseases in question than when it subsists on healthy plants.

Though classified as a single species, *Bemisia* is actually a complex of "biotypes", and biotype B, which arrived in China in the late 1990s, is rapidly taking the place over from the wimpy natives. Among the pathogens spread by whiteflies in China are tobacco curly shoot virus and tomato yellow leaf curl virus. These predate the arrival of biotype B, but the new arrival does particularly well on plants infected by them.

Dr Liu found that type B insects lived six times longer on infected plants than uninfected ones, and their population per infected plant might rise as high as 13 times that on an uninfected one. That mutualism does not seem to apply to the aboriginal whiteflies of China.

The virus, then, helps the insects multiply and in doing so helps itself to spread. Why that should be true only for this particular biotype is unknown. Finding the answer would make a lot of farmers happier.

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Neuroscience

Time of the month

Feb 1st 2007
From The Economist print edition

The reward circuitry in a woman's brain shifts with her menstrual cycle

THAT some women may just possibly get the teensy-weensiest bit prickly before their monthly periods is widely acknowledged. Though it is less well known, a woman's menstrual cycle can also affect her susceptibility to addictive drugs. The connection between the two may not be immediately obvious, but is probably to do with the effect of fluctuating levels of two sex hormones, oestrogen and progesterone, on the mood-producing parts of the brain.

To find out a bit more about what is going on as “that time of the month” approaches, Karen Berman and her colleagues at America's National Institute of Mental Health, in Maryland, put 13 female volunteers in a brain scanner. Their conclusion, just published in the *Proceedings of the National Academy of Sciences*, is that mood shifts do, indeed, coincide with shifting patterns of brain activity.

Dr Berman and her collaborators used a technique called functional magnetic-resonance imaging (fMRI), which is sensitive to changes in blood flow—and thus oxygen consumption—to measure how active particular parts of their volunteers' brains were. Their interest was in the anticipation of, and response to, rewarding stimuli (in this case, money). They made the volunteers play slot machines (or, rather, representations of slot machines depicted on a screen inside the scanner), on the understanding that the volunteers could keep part of the notional winnings from their gambles. That created the expectation—though not the certainty—of a reward each time the virtual wheels spun.

Crucially, each volunteer was examined twice in a month: once early in her menstrual cycle, before she had ovulated, and once late in the cycle, after ovulation but before the onset of menstrual bleeding. In the first case, only oestrogen is abundant in the bloodstream. In the second, progesterone is circulating, too.

Previous experiments have established that many parts of the brain are involved in anticipating and enjoying rewards. These include structures such as the amygdala, which have a wider role in regulating emotions and mood. Dr Berman found that almost all of these reward-associated regions are more active early in the menstrual cycle than late in it. In other words, in the days leading up to ovulation a woman's brain looks as though it is both primed to receive rewards and more appreciative of them when they arrive. After ovulation, the brain's readiness for both desire and enjoyment seems to fall away. Hence, possibly, premenstrual grumpiness. Although the researchers could not prove that these shifts are caused by hormonal changes, they are certainly correlated with them.

Such fluctuations in reward-circuit activity may also explain why women seem to be more sensitive to drugs like cocaine early in their cycles than later on. Previous work done at Columbia University found that if female addicts are treated with progesterone, both their craving for and their response to cocaine damp down. Put together with Dr Berman's observations, this suggests that early in the cycle, when there is little progesterone around but oestrogen is abundant, either some aspect of the reward circuit is vulnerable to corruption or a protective effect is lacking.

The fMRI method may shed light on severe premenstrual symptoms, too. Indeed, looking at women who suffer such symptoms is the team's next project. What it cannot do is explain why fluctuations in the reward circuit evolved. One possibility is that an enhanced anticipation of reward as a woman is approaching ovulation, and thus the most fertile time of her cycle, would increase her drive for sex or other pleasures. Getting the experiments needed to test that hypothesis past an ethics committee might, however, be tricky.

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Geomagnetism

A journey to the centre of the Earth

Feb 1st 2007
From The Economist print edition

Recreating the planet's magnetic field in a laboratory

HOW does the Earth's magnetic field originate? Sir Joseph Larmor, an Irish mathematician, proposed in 1919 that it was generated spontaneously by the swirling of molten metal inside the planet. His idea, though it later found favour, was ignored at the time. One problem was that it is extremely difficult to recreate the effect in the laboratory. But, almost 90 years after Larmor's paper, Stéphan Fauve of the Ecole Normale Superiéure in Paris and his colleagues have managed to do so. They have published their method in this week's issue of *Physical Review Letters*.

Creating a magnetic field using electricity is easy: an electric current flowing in a wire generates a magnetic field around that wire. Similarly, moving a magnet creates an electric current in a neighbouring wire. This is the basis of electric motors and dynamos respectively. But when it comes to using the turbulent flow of liquid metal rather than well-behaved cables and wires, the experiment becomes rather harder.

Dr Fauve's model of the Earth's core was a cylindrical tank some 50cm long filled with liquid sodium. To recreate the effect of heat flowing through the planet's interior, the researchers stirred this brew with iron paddles attached to iron discs placed at each end of the tank.

The discs whirred in opposite directions some 26 times a second. At this speed, the flow of the molten metal through the random, small magnetic fields that exist in all magnetic materials was such that it created an electric current that, in turn, generated a self-sustaining magnetic field. For such self-generation to occur, the flow of liquid sodium had to be both complex and rapid. This is because the metal has to be mixed both longitudinally and latitudinally, so that it tangles up the magnetic fields faster than they can untangle. That suggests a lot of rapid convection in the Earth's interior (though not as rapid as in Dr Fauve's simulation, since things are happening on a grander scale, and in liquid iron, not liquid sodium).

This result certainly clears up one mystery. But it leaves a second unresolved. Why does the field spontaneously reverse itself every few hundred thousand years? If Dr Fauve could mimic that in his sodium bath, it really would be a “eureka” moment.

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The Richard Casement internship

Feb 1st 2007
From The Economist print edition

We invite applications for the 2007 Richard Casement internship. This is for a would-be journalist to spend three months of the summer working on the newspaper in London, writing about science and technology. Our aim is more to discover writing talent in a science student or scientist than scientific aptitude in a budding journalist. Applicants should write a letter introducing themselves, along with an original article of about 600 words that they think would be suitable for publication in the Science and technology section. They should be prepared to come for an interview in London or New York, at their own expense, but a small stipend will be paid to the successful candidate. Applications must reach us by February 22nd. They should be sent by e-mail to casement2007@economist.com

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About sponsorship

German cinema

Baby snatching and dead-end jobs

Feb 1st 2007 | BERLIN
From The Economist print edition

German films are riding on a wave of critical and commercial acclaim as directors find that they can make people laugh—to everyone's surprise

AP

"WHEREVER I go in the world", says Dieter Kosslick, director of the Berlin film festival, "there is a real sense of excitement about German films." This optimism has been growing ever since "Good Bye Lenin!" became a hit in 2003, grossing $80m, most of it overseas. Wolfgang Becker's reunification tale, about a woman who falls into a coma just before the Berlin wall comes down and wakes up eight months later, had a bittersweet magic to it: a small human story illuminating a massive historical event. Virtually no German films were being sold abroad at the time, so its success came as a surprise. Audiences and critics outside Germany were amazed that German storytelling could be so light.

"Good Bye Lenin!" was also a strong contender in the Berlin film festival's main competition. Four years on, the festival, which runs from February 8th-18th, includes two new German-language offerings: "Yella", directed by 46-year-old Christian Petzold, and "Die Fälscher" ("The Counterfeiters"), about a money-printing scam at the end of the war, directed by Stefan Ruzowitzky, an Austrian film-maker.

German films do not automatically make the grade in this most important of European festivals (which is more accessible to the general public than its more glamorous rivals, Venice and Cannes). When German films appeared to be promoted beyond their worth, before and immediately after reunification, critics were invariably disparaging and audiences bored. The glory days of the 1960s and 1970s, when directors such as Werner Herzog and Rainer Werner Fassbinder were at their best, had vanished.

Then, in 2004, the year after "Good Bye Lenin!", Hamburg-born Fatih Akin, of Turkish parentage, won the festival's Golden Bear award for "Gegen die Wand" ("Head-On"), a bleak, violent tale about Turkish-German cultural crossover. "It was a fantastic kick for the industry to have 'Head-On' win," says Mr Kosslick.

Verena Lüken, a film critic at the *Frankfurter Allgemeine Zeitung*, one of the country's leading papers, notes that today's films squarely address those contemporary issues that matter most to Germans: migration, identity, social marginalisation and history. "The question asked by the new generation in these films is not the inevitable 'Was my grandfather a Nazi' but, say, 'Was my grandfather an Anatolian?'"

Ms Lüken remembers being tired by German fare throughout the 1980s and 1990s. Now, she says, people like her are glad to be able to "leave behind this really bad impression we had then. German critics sit up when they hear critics in France or England praising German movies."

Ever since "Good Bye Lenin!" and "Head-On", German cinema has grown in confidence. More films are being made. Film schools in Cologne and Berlin are thriving. Directors such as Valeska Grisebach and Benjamin Heisenberg, both under 40 and not known outside Germany, are being praised for films of genuine originality. And a new three-year

fund, worth €60m ($77.5m) a year and open to anyone making a feature film in Germany with a budget of at least €1m, has also just been established by the Ministry of Culture.

German film-makers have discovered that if you make your film entertaining and surprising, as happened with “Good Bye Lenin!”, you can succeed at the box office. Some are stories about very ordinary lives, as in the urban, edgy work of Andreas Dresen and Mr Petzold. Mr Dresen's “Sommer vorm Balkon” (“Summer in Berlin”), about two young women in dead-end jobs, lacks plot or any obvious action, but it works at another level: the idiosyncratically drawn characters, involved with unsuitable men, are impossible not to like. The film has an easy charm, something always expected of French films, but rare in German ones.

Mr Petzold's “Gespenster” (“Ghosts”), also set in a summery Berlin, is more sinister. A girl in care, Nina, is spotted by a French woman who believes her to be her baby, stolen years before from a supermarket trolley. We learn that the woman is ill, in long-term, traumatic mourning for her loss. Nina, also befriended by a sassy kleptomaniac called Toni who takes her on a thieving spree, is no one's daughter.

Here Mr Petzold taps into a compelling German theme: that of emptiness, of something missing, of one generation trying, and often failing, to connect with another. His film is a little similar to an earlier masterpiece, Wim Wenders's “Paris, Texas” (1984), only on a much smaller budget and with an unnerving naturalism.

These deliberately modest films, belonging to what is loosely termed the “Berlin school”, rub shoulders with more conventional, full-scale location movies. Many of them are made by Constantin Film, a Munich production company. One such was Oliver Hirschbiegel's 2004 “Der Untergang” (“Downfall”), about Hitler's last days, the most talked-about German film in decades.

Hoping for an Oscar

But the film that is currently causing the biggest stir is “Das Leben der Anderen” (“The Lives of Others”), about Stasi surveillance of an East Berlin writer set five years before the fall of the wall. It has already picked up numerous European prizes and has just been nominated for an Oscar for best foreign film. While its rookie director, Florian Henckel von Donnersmarck, struggled for eight years to get it made, there is little else about this wonderful film that is ostentatiously heroic. Quiet and poignant, it is also starkly authentic: this is how the GDR, with its bugging, wanton bureaucracy and petty cruelty, must have been.

Sebastian Koch is magnetic as Georg Dreyman, the lead. Martina Gedeck, Dreyman's compromised actress-girlfriend Christa-Maria, is engrossing and Ulrich Mühe (pictured), as the repressed, intruding Stasi officer who finally saves Dreyman through calculated acts of misinformation, is magnificent. The film is a real piece of authorship, chilling yet entirely believable.

If “The Lives of Others” wins its Oscar, as did another German film in 2002, “Nirgendwo in Afrika” (“Nowhere in Africa”), it will confirm a return to form for German films of substance and broad appeal. If it does not, no matter. Films as good as this will go on being made. People everywhere want to see them.

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New Arab fiction

Exile is another country

Feb 1st 2007
From The Economist print edition

Three new novels focus, with considerable success, on war, exile and grief

WHO would be an Israeli Arab? A non-Jew in a Jewish state; a citizen with most, but not all, civil rights (it is almost impossible for Arabs to buy state-owned land); regarded with suspicion by many Jewish Israelis; envied, disliked, even labelled as traitors by Palestinians on the other side of the 1967 border: this is not a fate that many people would choose.

Yet despite these burdens, Israel's Arab minority (or "Palestinian citizens of Israel" as many now define themselves) enjoy the greatest civil and political freedoms in the Middle East. In "Let It Be Morning", a provocative and memorable novel first published in America last year and only now coming out in Britain, Sayed Kashua, an Arab journalist for *Haaretz*, a left-wing Israeli newspaper, exploits them to the full.

Mr Kashua's narrator is also a young Arab journalist, returning to his home village with his wife and baby in search of a quiet life. He has been steadily marginalised on his paper, downgraded from a staff position to contributor, his desk taken over by the fashion department. Mr Kashua is sharp, if bleak, on the narrator's growing self-loathing as he tries without success to ingratiate himself with his supposedly liberal editors.

But things are anything but quiet when the Israeli army blockades the village. Water and electricity supplies are cut off. Telephone lines and the mobile network stop working. Even the sewage pipes are sealed. Society, and the everyday bonds of community, rapidly collapses. Neighbour turns on neighbour, and the mob takes over the streets. The village elders, seeking to appease the Israelis, round up the illegal Palestinian workers, strip them to their underwear and force them to march towards the Israeli lines where a number of them are shot and killed.

Mr Kashua's pacy narrative keeps the story moving to a clever and blackly humorous climax. The water and power are turned back on. The telephone lines work. The village, it turns out, is no longer part of Israel but has been handed over to Palestinian control under the terms of a secret peace treaty. Its inhabitants greet the news not with jubilation, but with horror. "The Jews have sold us down the river," shouts the furious grocer.

Samir El-Youssef is a Palestinian, born in Rashidia refugee camp in Lebanon. Like Mr Kashua, Mr El-Youssef is interested in exploring present-day scenarios rather than the refugee camps' myths that the old Palestine will be reborn. Mr El-Youssef co-authored "Gaza Blues", a well-received collection of short stories, with an Israeli author, Etgar Keret. His first novel, dedicated to a British Jewish novelist, Linda Grant, is a slim but potent meditation on memory and exile.

"The Illusion of Return" is rich in double meaning: the first illusion is that the Palestinians can ever return to their home villages, many of which now lie buried under Israeli housing estates and industrial parks. The second explores the question of whether anyone can properly revisit the past, even if just in their own memory.

The narrator meets his friend Ali at London's Heathrow airport, after a gap of 17 years. Both are haunted by the past in Lebanon: the narrator's beloved sister Amina killed herself, while Ali became an Israeli collaborator. The first-person narrative cuts back between the past and present, which sometimes results in too much "telling" rather than "showing". But Mr El-Youssef's vivid portrait of life in wartime Lebanon, and the temporary refuge provided by friends, is poignant and evocative. It is left to Bruno, an elderly Holocaust survivor, to help Ali find some inner peace. "Life", he says, "is a one-way journey: there is no going back."

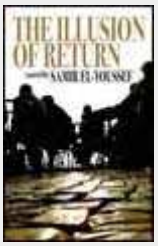
Except sometimes there is. In "Dreams of Water", Aneesa, a young Lebanese woman, flees Beirut for London after

Let It Be Morning
By Sayed Kashua. Translated by Miriam Shlesinger

Grove Press; 288 pages; $13.
Atlantic Books; £8.99

Buy it at
Amazon.com
Amazon.co.uk

The Illusion of Return
By Samir El-Youssef



Halban; 154 pages; £12.99

Buy it at
Amazon.co.uk

Dreams of Water
By Nada Awar Jarrar

HarperCollins; 240 pages; £14.99

Buy it at
Amazon.co.uk

her brother Bassem is kidnapped and is never seen again. Crazed with grief, Aneesa's mother adopts a young boy who looks like Bassem, believing that he is her son's reincarnation. Adrift in London, Aneesa finds friendship, even platonic love, with Salah, an elderly Lebanese man. Their relationship is touchingly drawn, as they take excursions in the rain, longing for the tastes of home and the tang of the Mediterranean, but grateful that nobody is shooting at them.

This beautifully written book is powerfully evocative of the human cost of war and the longing for love that, despite the shooting and shelling, never fades. As with much of the literature of exile, the city itself is a character. Ms Jarrar's descriptions of Beirut—the fishermen on the Corniche, the palm trees waving in the sea breeze, the wind flowing through the apartment buildings—are both lyrical and precise. Eventually, Aneesa returns to Beirut and to her mother. All human bonds are transitory, it seems, except those of blood. Together, mother and daughter find a kind of peace. Each of these novels touches the reader's heart. Exile and displacement, whether within one's homeland, or outside, may be painful, but it can also inspire fine literature.

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By Sayed Kashua. Translated by Miriam Shlesinger.
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Balkan history

Fighting and looting

Feb 1st 2007
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LAST year Montenegro became the world's newest state. In a few years' time it hopes to join the EU, along with its neighbours. Although it has a tiny population, Montenegro also has as rich and violent a past as anywhere else on the continent. And Montenegrins themselves have a strong sense of history. In 1991 as they sacked and burned villages around Dubrovnik, your correspondent was struck by the sense of just how much these men felt that fighting and looting were preordained by history, something their fathers, grandfathers and great-grandfathers had done before them and their sons would do again in future.

So it is perhaps all the more surprising that no general history of Montenegro, except for ones written by Montenegrins, has been published abroad since 1912. There was a very large gap to be filled, albeit for a very small place.

Elizabeth Roberts, a former diplomat who has taught Balkan history, has filled it. Now that she has produced such a thorough book, future historians may not bother again: if one history was enough for the last century, perhaps one is enough for this century too.

Much of the book is not specifically about Montenegro. That is unavoidable. Montenegrin history is so intertwined with the Serbian, Yugoslav, Dalmatian and Balkan stories that it is impossible to look at it in isolation. In the second world war Montenegrin partisans were forever weaving in and out of Serbia and Bosnia. Likewise, arguably the best known Montenegrin of the last century, Milovan Djilas, a staunch communist, spent much of his life in prison or at home in Serbia.

For centuries too the Montenegrins have been adept at manoeuvring between the great powers. During the late 1990s their government secured more American aid per head of population than any other country, bar Israel. The Montenegrins have successfully fought, allied with or been subsidised by the Ottomans, Venetians, Russians, British, French, Serbs, Albanians, Austrians, Bosnians, Italians, Germans, other (former) Yugoslavs, the EU and America.

Today's modern state is far larger than historic Montenegro, which for centuries was ruled as a theocracy by a prince-bishop. In 1807 one of Napoleon's generals was sent to remonstrate with the then incumbent over the local practice of chopping prisoners' heads off, including, allegedly, that of a French general whose head was then used as a football. Napoleon's man was sent away with a flea in his ear. After all, the prince-bishop pointed out, had not the French only recently chopped off the heads of their own king and queen in a square in Paris?

Although Ms Roberts makes a valiant attempt to turn the sweep of Montenegrin history away from war, banditry and looting to discuss its (modest) contributions to literature and the theme of Montenegrin identity, she cannot get away from the fact that its history has been bloody in the extreme. Today Britons, Irish and Russians are leading a new invasion of the country, buying holiday homes. This book may leave them wondering if looting is covered by their insurance.

Realm of the Black Mountain: A History of Montenegro.
By Elizabeth Roberts.
Hurst; 521 pages; £25.
To be published in America by Cornell University Press in March

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New fiction

Black dog

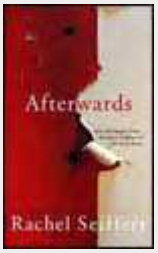
Feb 1st 2007
From The Economist print edition

RACHEL SEIFFERT'S first novel, “The Dark Room”, which was shortlisted for the Man Booker prize in 2001, told the stories of three ordinary Germans and how the second world war impinged upon their lives. In the same intelligent, understated way, her new book, “Afterwards”, reaches parts that are equally if not more morally complex: the soldier's re-entry into civilian life and the toll upon the human spirit of guilt, fear, anger and silence at the shedding of blood.

Alice and Joseph are two young, hopeful Londoners. She is a nurse, he a painter and decorator. Both carry a backpack of emotional baggage. Alice's absent father casts a shadow over her life, while the grandmother who helped raise her has recently died.

Joseph seems as serious as she is about their new relationship. Yet there is something withheld about him that shows itself in long silences and the occasional going AWOL. Joseph clams up when questioned about his army experiences in Northern Ireland. Whether he is unwilling or unable to speak about what happened there is unclear, but it makes Alice feel shut out. When Alice's widowed grandfather begins to open up about the months during the 1950s that he spent bombing Mau Mau insurgents hiding in Kenya's Aberdare mountains, Joseph's pent-up emotion boils over.

Afterwards
By Rachel Seiffert



To be published in America by Pantheon in July
William Heinemann; 327 pages; £14.99.

Buy it at
Amazon.com
Amazon.co.uk

To use painting and decorating—stripping off wallpaper, cutting out damp skirting—as a symbol of cleansing the soul is risky. In the hands of any but the subtlest writer, this is so obvious a metaphor as to be unworkable. But Ms Seiffert has the lightest of touches. And she is as good at finding the words men use to anaesthetise themselves in the brute callousness of war as she is at navigating the tentativeness of new lovers undressing for the first time.

Readers who wonder why writers as talented as Martin Amis and the 2006 Man Booker prize-winner, Kiran Desai, seem to flinch from writing about their own times should study Ms Seiffert. There is nothing easy or obvious about this work; she has lessons for us all.

Afterwards.
By Rachel Seiffert.
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Russian emigrés

A fine turncoat

Feb 1st 2007
From The Economist print edition

LIKE a Jew becoming a Nazi, was how her relatives saw it. How could a brainy, sensitive woman, exiled from her homeland by a monstrous totalitarian regime that hounded her class and murdered her friends and relatives, become an unflinching supporter of its creed?

That is the puzzling life of the beautiful Sofka Dolgorouky. Born into one of tsarist Russia's grandest families, she escaped from Soviet clutches only to spend the second world war in a Nazi internment camp. Sexually insatiable, she had two husbands and countless lovers, and neglected her children abominably. After all that, she ended up happily but squalidly in a cottage in a remote corner of rural England, defiantly communist to the last.

The story is told by her granddaughter, Sofka Zinovieff, who maintains an appropriate tone of slightly bemused sympathy with her captivating but repellent subject. She retraces her grandmother's footsteps, in Russia, France and Britain, presenting an evocative mix of past and present, partly with her own acute descriptions, and partly from her documentary sources. These include the copious diaries and notes of Mrs Skipwith (née Princess Dolgorouky), the recollections (mostly caustic) from the rest of the family and some revealing files from the British security service, who tracked their exotic Russian target (“outstandingly intelligent, courageous and active”) through the shabby grey world of post-war London.

Red Princess: A Revolutionary Life
By Sofka Zinovieff

Granta; 346 pages; £16.99

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Like the men in raincoats, Ms Zinovieff fails in the probably impossible task of explaining how someone who had suffered so much from totalitarianism could embrace an ideology that upheld it. The horrors of Soviet policy at home and abroad, exposed time after time from 1917 onwards, gradually destroyed the hopes and convictions of sympathisers with the Bolsheviks' experiment, even in the British Communist Party. But it left her grandmother's faith intact. You couldn't blame Christianity for Torquemada, and you shouldn't blame socialism for Stalin, was her usual answer.

The easy explanation is that her judgment was scarred by the poverty she witnessed in the 1930s, and by living on the fringes of the Holocaust—the Jews in her internment camp perished in Auschwitz. But others who experienced the same horrors became ardent democrats; the princess after the war became an enthusiastic tour-guide to the countries of the communist bloc, even editing a magazine that glorified the Stalinist outpost of Albania.

A second puzzle is that someone so good at making friends was so careless with her relatives. Ms Zinovieff reluctantly concedes that her grandmother was not just chronically unfaithful but wildly promiscuous (“bedding” was her own word for casual sex); worse, her hapless children were left in strange hands for long periods, and then moved with a cruel abruptness that even the kindest biographer can hardly excuse. Her self-absorbed carelessness in that, and towards money, hygiene and much more besides, make it easy to see why her Russian in-laws loathed the turncoat princess. Yet anyone reading about her sizzling charm, guts and literary gifts can't help thinking it would have been fun to know her.

Red Princess: A Revolutionary Life.
By Sofka Zinovieff.
Granta; 346 pages; £16.99

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New cinema

Two-handed combat

Feb 1st 2007
From The Economist print edition

Of Clint Eastwood's two films about Iwo Jima, the Japanese is far better

IN TRADITIONAL war films, the enemy is faceless. Imbuing opponents with humanity would rob “our boys” and the audience of moral certitude. Reality is different. There is no glory in war and the boys on both sides—and so many are just boys—are human; terrified and unsure about what they are fighting for. Clint Eastwood, a Hollywood actor and director, has provided a powerful reminder of this by making two films of the same battle.

The conquest of Iwo Jima, shown from an American view in “Flags of our Fathers” and from the Japanese side in “Letters from Iwo Jima”, was the most brutal and pointless of the second world war. By February 1945, it was clear that the Allies' technological and numerical superiority was unbeatable. Yet the Japanese, led by an inspired general, dug themselves in on Iwo Jima, a bleak, volcanic island far from Tokyo. It took American marines five weeks to overrun them. Some 7,000 Americans and 22,000 Japanese died. But what turned Iwo Jima into legend was Joe Rosenthal's photograph of six American soldiers raising a flag on Mount Suribachi.

Imagenet

Goodbye to all that

The first film, which opened last October, follows the fate of those flag raisers. Three are killed in the subsequent combat, since the flag was raised on the fifth day of battle and not at the end, as the American public believed. The others, including James “Doc” Bradley, whose son's book is the basis for the film, are sent home to drum up enthusiasm for war bonds. The tawdriness of their public-relations tour, which has them climbing a cardboard Mount Suribachi to cheering crowds, proves more corrosive than the horrors of battle. One of the three dies an alcoholic.

Mr Eastwood's point that war heroes are cynically manufactured is well made. Seemingly aimed at the current Iraq war, it is ironic then that it turns a film about propaganda into propaganda itself. That war is romanticised is hardly new, as Wilfred Owen's first world war poetry and Robert Capa's 1936 “falling soldier” photograph attest. In the end, polemic dulls this film, leaving it oddly insubstantial—its characters too little developed for us to care.

Not so for “Letters from Iwo Jima”, which opens in America next week and in Europe at the end of February. The film is rich with memorable individuals: Saigo, a humble baker who misses his wife and baby daughter; Baron Nishi, an Olympic gold medallist equestrian who brings his horse to the island; and their wise leader General Kuribayashi, a patriot who nevertheless respects his American foes. The discovery of his letters home in a cave on Iwo Jima sparked Mr Eastwood's interest. The film's more conventional narrative brings the characters to life and embraces nuance: daring to show not just the fanatical Imperial Army soldiers blowing themselves up with grenades rather than surrendering, but also marines shooting Japanese prisoners rather than guarding them.

It is possible to do terrible things only to faceless foes. Ultimately, and laudably, Mr Eastwood's films attack anonymity, whether invisible enemy or fake heroes. In one of the film's most moving scenes, Baron Nishi reads his men a letter sent to a captured American marine from his mother. As the Japanese soldiers realise that he is just like them, the fog of war lifts to reveal a shared humanity.

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Abbé Pierre

Feb 1st 2007
From The Economist print edition

Henry Grouès (“Abbé Pierre”), champion of the homeless, died on January 22nd, aged 94

AFP

TRADITIONALLY most saints are gentle creatures. Those enshrined in French homes, or on prayer-cards stuffed into the missals of elderly churchgoers, are usually St Anthony carrying the child Jesus, or smiling St Thérèse of Lisieux with a bouquet of flesh-tinted roses. Odd, then, that the nearest modern France has come to a saint was a man fuelled and driven by unceasing anger: anger that the poor should suffer and that the rich did not care.

For any man in authority, clerical or lay, a visit from Abbé Pierre was an unsettling experience. First there was the look of him: the *coupe zéro* haircut under a black beret, the straggling beard, the black cape thrown dramatically across the shoulders, the belted soutane and muddy boots from tramping through slums. Then came the disquieting blue stare, and the surprisingly loud, ringing voice. He was not a large man or a strong one: lung trouble had disrupted his studies as a boy, and he had been advised at 26 to give up the monastic life for his health's sake. His anger surprised even himself; it did not seem in character. But it made him a giant.

Charles de Gaulle summoned him in 1945, after giving him the Croix de Guerre for a brave, clandestine war, to have an appreciative word; Abbé Pierre lectured him on the lack of milk for babies. Almost 50 years later, the elderly priest refused to wear his Légion d'honneur until a crowd of 300 poor African families, sleeping rough on the esplanade de Vincennes in Paris, was given lodging. When Jacques Chirac, hoping to score electoral points, offered to open up empty buildings for the homeless, Abbé Pierre berated him for hypocrisy. With “measured insolence”, he scolded John Paul II for not allowing married priests and for refusing to retire. He would bite people's ears like a flea, he said, and yell, “Wake up!”

France first heard that voice at lunchtime on February 1st 1954. The napkins were tucked in, the spoons poised over the soup, when Abbé Pierre, having seized the microphone at Radio Luxembourg, told his listeners that a woman had frozen to death that night on the boulevard Sebastopol. She had been clutching an eviction notice, served to her the day before. The weather was grim; all over France, thousands more were dying. Abbé Pierre appealed for blankets, food, stoves and money to be brought to his temporary headquarters at the Hotel Rochester. The response was so enormous that not only the hotel lobby, but the disused Gare d'Orsay nearby, were filled to the roof with donations. Army lorries helped distribute them, and the National Assembly voted 10 billion francs for housing for the poor.

The organisation to which the rich brought their jewellery, and ordinary people packets of rice and jars of jam, was still a strangely fluid affair. It was run from a large ramshackle house in Neuilly-Plaisance, a Paris suburb, where Abbé Pierre in 1949 had started taking in the homeless, first in rooms and then, as numbers grew, in shacks in the garden. He had no idea what this project would become. Perhaps it would be no more than a kindly bourgeois gesture, the sort his own wealthy father had made when he went, each Sunday, to wash and shave the poor in the shelters of Lyon.

His colleagues were a strange, quarrelsome band, ex-cons and ex-legionnaires, some of whom had been homeless themselves. To raise funds they picked rags and salvaged furniture, or begged with laundry baskets in the Paris

streets. Abbé Pierre called his project “Emmaus”, after the place where two disciples had given shelter to the risen but unrecognised Christ.

Love human, love divine

Emmaus communities caught on and thrived; by 2006 there were 350 of them in nearly 40 countries, 110 in France itself. Abbé Pierre became a thorn in the side of successive French governments, and a year before he died was still lobbying for a law establishing the right to lodging. Yet he did not relish publicity on his own account. After regularly topping the annual poll of best-loved figures in France, in 2004 he asked to be removed from it. Celebrity helped the cause, but it appalled him.

He had little enough to hide: a clutch of Utopian left-wing views, and one dismaying brush with Holocaust denial which seemed the mere misjudgment of old age. In 2005 he also admitted, in a memoir, that chastity was too hard for him. He had decided to become a monk at 15, and had joined the Capuchins at 19; from then on, the pain of living without sexual love was constant. Indeed, he did not always live without it. He occasionally slept with women and would sometimes, wistfully and innocently, fall into discussions of sex with women who scarcely knew him.

Yet those who imagined him deprived of love were wrong. Abbé Pierre was possessed by it. Priest though he was, he rarely preached or mentioned God by name, a fact that only added to his popularity in proudly secular France. The force he invoked was different. “Despite all the evil that men and women suffer”, he said once, “I believe that the Eternal is Love all the same, and we are loved all the same, and we are free all the same.” Love would absorb him in the end, when his “Sister Death” came, as tenderly as any woman, to embrace him. And it was Love, he said, that made him so angry.

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Overview

Feb 1st 2007
From The Economist print edition

In **America** GDP grew at an annual rate of 3.5% in the fourth quarter, according to preliminary figures, despite a sharp fall in residential investment. In the year as a whole, GDP rose by 3.4%, up from 3.2% in 2005. The Federal Reserve left interest rates at 5.25% on January 31st, after a two-day rate-setting meeting. The Fed said that "inflation pressures seem likely to moderate over time," but added that "some inflation risks remain."

Consumer prices in **Japan** rose by 0.1% in December, leaving the headline inflation rate unchanged at 0.3%. Excluding food and energy, prices declined by 0.3% in the year to December. Industrial production rose by 0.7% in the month and by 4.6% from a year earlier. Japan's unemployment rate inched up from 4.0% to 4.1%.

The **euro area's** unemployment rate edged down to 7.5% in December, helped by another big tumble in German joblessness, to 9.5%, and a fall in France's rate, to 8.6%. Inflation in the euro area was unchanged, at 1.9% in January.

German retail sales data are notoriously unreliable, but suggest that shoppers tried to beat this month's rise in value-added tax. Excluding cars and purchases at petrol stations, sales rose by 2.4% in December.

Booming investment helped **Russia's** GDP grow by 6.7% last year.

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About sponsorship

Output, prices and jobs

Feb 1st 2007
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2006†	2007†	latest	latest	year ago	2007†	rate‡, %
United States	+3.4 Q4	+3.5	+3.3	+2.2	+3.0 Dec	+2.5 Dec	+3.4	+2.0	4.5 Dec
Japan	+1.6 Q3	+0.8	+2.3	+1.9	+4.6 Dec	+0.3 Dec	–0.4	+0.4	4.1 Dec
China	+10.4 Q4	na	+10.5	+9.4	+14.9 Nov	+2.8 Dec	+1.6	+2.1§	9.8 2006
Britain	+3.0 Q4	+3.2	+2.6	+2.4	+0.8 Nov	+3.0 Dec**	+1.9	+2.2	5.5 Nov††
Canada	+2.5 Q3	+1.7	+2.8	+2.4	–2.2 Nov	+1.6 Dec	+2.2	+2.0	6.1 Dec
Euro area	+2.7 Q3	+2.0	+2.7	+2.0	+2.5 Nov	+1.9 Jan	+2.4	+2.1	7.5 Dec
Austria	+3.2 Q3	+3.6	+2.8	+2.3	+5.6 Nov	+1.5 Dec	+1.6	+1.6	4.7 Dec
Belgium	+3.1 Q3	+2.5	+2.8	+2.1	nil Nov	+1.7 Jan	+2.6	+1.8	11.7 Dec‡‡
France	+1.9 Q3	nil	+2.0	+2.0	–1.1 Nov	+1.5 Dec	+1.5	+1.4	8.7 Nov
Germany	+2.8 Q3	+2.6	+2.6	+1.6	+6.0 Nov	+1.6 Jan	+2.1	+2.1	9.5 Jan
Greece	+4.4 Q3	na	+4.1§	+3.5§	–1.8 Nov	+2.9 Dec	+3.6	+2.8§	8.3 Q3
Italy	+1.7 Q3	+1.1	+1.8	+1.2	+2.2 Nov	+1.9 Dec	+2.0	+1.9	6.8 Q3
Netherlands	+2.7 Q3	+2.8	+2.8	+2.3	+3.7 Nov	+1.1 Dec	+2.0	+1.7	5.2 Dec††
Spain	+3.8 Q3	+3.6	+3.6	+3.0	+4.2 Nov	+2.7 Dec	+3.7	+2.7	8.5 Dec
Czech Republic	+5.8 Q3	+5.6	+6.0	+4.8	+7.6 Nov	+1.7 Dec	+2.2	+3.3	7.7 Dec
Denmark	+3.2 Q3	+2.9	+3.3	+2.3	+7.9 Nov	+1.8 Dec	+2.2	+1.9	3.9 Dec
Hungary	+3.8 Q3	+4.2	+3.7	+2.4	+10.8 Nov	+6.5 Dec	+3.3	+5.9	7.5 Oct-Dec††
Norway	+2.6 Q3	+5.2	+2.5§	+2.3§	–5.8 Nov	+2.2 Dec	+1.8	+2.6§	3.1 Nov††
Poland	+5.8 Q3	na	+5.3	+4.7	+5.7 Dec	+1.4 Dec	+0.7	+2.5§	14.9 Dec‡‡
Russia	+6.5 Q3	na	+6.7	+6.5	+1.9 Dec	+9.1 Dec	+10.9	+9.2§	6.7 Nov‡‡
Sweden	+4.4 Q3	+4.1	+4.6	+3.3	+6.2 Nov	+1.6 Dec	+0.9	+1.9	4.6 Dec‡‡
Switzerland	+2.4 Q3	+1.5	+2.8	+2.0	+8.2 Q3	+0.6 Dec	+1.0	+1.0	3.3 Dec‡‡
Turkey	+3.4 Q3	na	+5.2	+4.0	+10.9 Nov	+9.7 Dec	+7.7	+8.6§	9.1 Q3‡‡
Australia	+2.2 Q3	+1.2	+2.5	+2.9	+0.9 Q3	+3.3 Q4	+2.8	+2.8	4.6 Dec
Hong Kong	+6.8 Q3	+14.8	+6.0	+5.0	–0.6 Q3	+2.3 Dec	+1.3	+2.5§	4.4 Dec††
India	+9.2 Q3	na	+8.3	+7.4	+14.4 Nov	+6.3 Nov	+5.3	+6.1§	7.6 2006
Indonesia	+5.5 Q3	na	+5.3	+5.8	–4.8 Oct	+6.3 Jan	+17.0	+6.6§	10.3 2005
Malaysia	+5.9 Q3	na	+5.5	+5.2	+7.2 Nov	+3.1 Dec	+3.5	+3.4§	3.1 Q3
Pakistan	+6.6 2006§§	na	+6.2§	+6.6§	+6.8 Sep	+8.9 Dec	+8.5	+7.0§	na
Singapore	+5.9 Q4	+7.6	+7.7	+5.0	+5.1 Dec	+0.8 Dec	+1.3	+1.0§	2.6 Q4
South Korea	+4.0 Q4	+3.4	+4.9	+4.2	+2.3 Dec	+1.7 Jan	+2.2	+2.3§	3.3 Dec
Taiwan	+5.0 Q3	na	+4.1	+3.9	–1.7 Dec	+0.7 Dec	+2.2	+1.5§	3.9 Dec
Thailand	+4.7 Q3	+6.0	+4.3	+4.3	+7.0 Dec	+3.0 Jan	+5.9	+3.6§	1.2 Nov
Argentina	+8.7 Q3	+10.8	+7.9	+6.3	+3.8 Nov	+9.8 Dec	+12.3	+9.8§	10.2 Q3‡‡
Brazil	+3.2 Q3	+1.4	+3.0	+3.3	+4.2 Nov	+3.1 Dec	+5.7	+3.7§	8.4 Dec‡‡
Chile	+2.9 Q3	–0.2	+4.7	+5.3	+1.2 Dec	+2.6 Dec	+3.7	+2.3§	6.0 Dec†††‡
Colombia	+7.7 Q3	+8.1	+5.1	+4.5	+17.4 Oct	+4.5 Dec	+4.9	+4.2§	11.0 Nov‡‡
Mexico	+4.6 Q3	+4.1	+4.4	+3.2	+4.8 Nov	+4.1 Dec	+3.3	+3.8§	3.5 Dec‡‡
Venezuela	+10.2 Q3	na	+7.8	+5.5	+12.2 Sep	+17.0 Dec	+14.3	+17.0§	10.1 Q3‡‡
Egypt	+7.1 Q3	na	+5.5	+5.4	+4.0 2005	+12.4 Dec	+3.1	+6.5§	10.9 Q2‡‡
Israel	+4.6 Q3	–1.1	+4.2	+4.2	+13.2 Nov	–0.1 Dec	+2.4	+1.7§	8.3 Q3
Saudi Arabia	+5.3 2006§	na	+5.3§	+5.4§	na	+2.7 Oct	+0.9	+2.0§	na
South Africa	+4.5 Q3	+4.7	+4.3	+4.2	+5.4 Nov	+5.8 Dec	+3.6	+5.6§	25.6 Mar‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	+11.6 Q3	+11.7	+10.7§	+8.9§	+4.8 Nov	+5.1 Dec	+3.6	+3.8§	4.5 Nov
Finland	+5.8 Q3	+3.6	+4.5§	+2.7§	+5.4 Nov	+2.2 Dec	+1.0	+1.9§	7.3 Dec
Iceland	+0.3 Q3	+0.4	+3.7§	+0.7§	na	+6.9 Jan	+4.4	+5.4§	1.1 Nov‡‡
Ireland	+7.7 Q3	+10.8	+5.8§	+5.3§	–10.8 Nov	+4.9 Dec	+2.5	+3.4§	4.5 Dec
Latvia	+11.8 Q3	na	+10.8§	+8.0§	+0.7 Nov	+6.8 Dec	+7.0	+5.2§	6.2 Nov
Lithuania	+6.6 Q4	nil	+7.3§	+6.5§	na	+4.5 Dec	+3.0	+4.4§	5.7 Dec
Luxembourg	+5.4 Q3	+4.1	+5.5§	+4.3§	–0.4 Sep	+2.3 Dec	+2.5	+1.8§	4.6 Nov‡‡
New Zealand	+1.3 Q3	+1.0	+1.9§	+1.8§	–1.4 Q3	+2.6 Q4	+3.1	+3.0§	3.8 Q3
Peru	+6.9 Nov	na	+6.0	+5.4	+9.4 Oct	+1.1 Dec	+1.5	+2.2§	8.5 Nov‡‡
Philippines	+4.8 Q3	+1.3	+5.5	+5.3	–19.2 Oct	+4.3 Dec	+6.7	+5.1§	8.0 Q3‡‡
Portugal	+1.5 Q3	–0.6	+1.2§	+1.4§	+5.5 Nov	+2.5 Dec	+2.6	na	7.4 Q3‡‡
Slovakia	+9.8 Q3	na	+7.5§	+6.1§	+9.8 Nov	+4.2 Dec	+3.7	na	12.3 Nov
Slovenia	+5.6 Q3	na	+4.5§	+4.0§	+8.3 Nov	+2.8 Dec	+2.3	na	8.6 Nov‡‡

*% change on previous quarter, annual rate. †The Economist poll. ‡National definitions. §Economist Intelligence Unit estimate/forecast. **RPI inflation rate 4.4% in Dec. ††Latest three months. ‡‡Not seasonally adjusted. §§Year ending June.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

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About sponsorship

The Economist commodity price index

Feb 1st 2007
From The Economist print edition

The Economist commodity-price index

2000=100

	Jan 23rd	Jan 30th*	% change on one month	% change on one year
Dollar index				
All items	186.9	184.9	−1.1	+18.0
Food	157.5	155.5	−1.2	+13.3
Industrials				
All	225.0	223.0	−1.0	+22.5
Nfa†	152.9	155.2	+5.0	+4.2
Metals	264.4	259.9	−2.8	+29.9
Sterling index				
All items	142.7	143.0	−0.6	+6.9
Euro index				
All items	132.6	132.0	+1.3	+10.5
Gold				
$ per oz	645.70	645.67	+0.8	+13.3
West Texas Intermediate				
$ per barrel	53.69	56.81	−6.5	−16.2

*Provisional †Non-food agriculturals.

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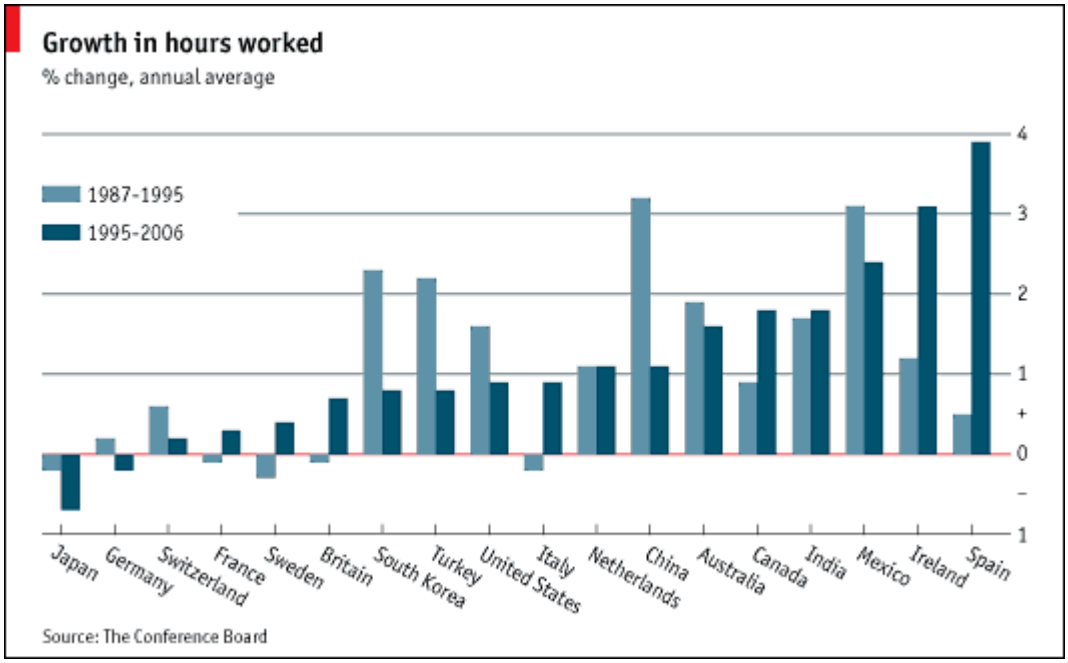
Growth in hours worked

Feb 1st 2007
From The Economist print edition

Infographics



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About sponsorship

Trade, exchange rates, budget balances and interest rates

Feb 1st 2007
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2007†	Currency units, per $ Jan 31st	Currency units, per $ year ago	Budget balance % of GDP 2007‡	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−837.2 Nov	−880.3 Q3	−6.3	–	–	−2.3	5.18	4.82
Japan	+79.6 Nov	+171.1 Nov	+3.8	121	118	−4.8	0.45	1.69
China	+177.5 Dec	+160.8 2005	+6.7	7.77	8.06	−1.9	2.95	3.10
Britain	−152.2 Nov	−69.7 Q3	−2.8	0.51	0.56	−2.7	5.56	4.97
Canada	+49.8 Nov	+28.9 Q3	+1.1	1.18	1.14	0.7	4.17	4.18
Euro area	−15.7 Nov	−31.4 Nov	−0.1	0.77	0.83	−1.7	3.78	na
Austria	−1.1 Nov	+12.2 Q3	+1.4	0.77	0.83	−1.4	3.78	4.08
Belgium	+14.8 Nov	+6.8 Sep	+2.2	0.77	0.83	0.1	3.83	4.09
France	−36.1 Nov	−43.0 Nov	−1.1	0.77	0.83	−2.5	3.78	4.08
Germany	+203.0 Nov	+121.5 Nov	+3.9	0.77	0.83	−1.7	3.78	4.05
Greece	−42.4 Oct	−28.8 Nov	−7.1‡	0.77	0.83	−2.9	3.78	4.31
Italy	−27.1 Nov	−43.5 Nov	−1.8	0.77	0.83	−3.5	3.78	4.26
Netherlands	+39.4 Nov	+63.2 Q3	+7.8	0.77	0.83	0.6	3.78	4.07
Spain	−112.8 Nov	−103.9 Oct	−8.5	0.77	0.83	0.6	3.78	4.09
Czech Republic	+2.0 Nov	−5.2 Q3	−2.7	21.6	23.5	−4.0	2.62	3.85
Denmark	+6.9 Nov	+7.2 Nov	+2.2	5.74	6.17	3.0	3.96	4.02
Hungary	−2.8 Nov	−6.9 Q3	−5.9	197	208	−7.1	8.20	7.24
Norway	+57.3 Dec	+56.0 Q3	+17.6‡	6.26	6.67	19.3	4.14	4.52
Poland	−4.1 Nov	−6.5 Nov	−2.3	3.01	3.16	−2.5	4.19	5.13
Russia	+140.8 Nov	+95.6 Q4	+7.3	26.5	28.1	5.9	10.50	6.30
Sweden	+20.7 Dec	+26.2 Q3	+6.4	6.97	7.64	2.4	3.20	3.99
Switzerland	+9.4 Dec	+105.9 Q3	+13.4	1.25	1.28	1.2	2.19	2.62
Turkey	−53.2 Nov	−33.7 Nov	−6.6	1.41	1.32	−2.8	19.17	18.91
Australia	−9.4 Nov	−39.5 Q3	−5.2	1.29	1.32	1.1	6.39	5.93
Hong Kong	−17.9 Dec	+19.2 Q3	+9.3	7.81	7.76	1.1	4.11	4.08
India	−51.7 Dec	−13.7 Q3	−2.2	44.2	44.1	−4.3	7.37	8.02
Indonesia	+38.5 Nov	+7.0 Q3	+1.4	9,100	9,325	−0.9	9.33	6.36§
Malaysia	+28.6 Nov	+22.2 Q3	+11.1	3.50	3.75	−4.1	3.68	5.43§
Pakistan	−12.9 Dec	−6.0 Q3	−5.1‡	60.7	59.9	−4.6	10.26	6.75§
Singapore	+33.1 Dec	+39.0 Q3	+25.2	1.54	1.63	0.3	3.38	3.16
South Korea	+16.4 Jan	+6.2 Nov	nil	942	962	0.4	4.96	5.00
Taiwan	+21.3 Dec	+26.3 Q3	+5.0	32.9	32.0	−2.8	1.82	2.08
Thailand	+2.2 Dec	+3.2 Dec	nil	34.7	39.2	−1.2	5.03	4.75
Argentina	+12.4 Dec	+6.7 Q3	+1.6	3.11	3.06	1.4	10.06	na
Brazil	+46.1 Dec	+13.5 Dec	+0.3	2.13	2.21	−2.2	12.93	6.16§
Chile	+22.1 Dec	+5.2 Q3	+2.2	544	528	5.8	5.04	5.37§
Colombia	+0.3 Oct	−2.3 Q3	−2.1	2,254	2,267	−1.5	6.82	6.34§
Mexico	−5.8 Dec	−1.3 Q3	−1.1	11.0	10.4	−0.3	7.05	7.92
Venezuela	+36.8 Q3	+29.7 Q3	+10.1	4,307	2,681	−2.5	10.09	6.55§
Egypt	−11.1 Q2	+3.5 Q2	+1.1	5.70	5.73	−8.0	9.44	5.51§
Israel	−7.9 Dec	+6.7 Q3	+1.5	4.26	4.67	−2.9	4.61	5.10
Saudi Arabia	+125.6 2005	+90.0 2005	+25.7‡	3.75	3.75	16.8	4.97	na
South Africa	−9.8 Dec	−13.5 Q3	−4.9	7.25	6.11	−2.0	9.40	7.78
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Estonia	−3.3 Nov	−2.1 Nov	−11.1‡	12.0	12.9	0.7	na	na
Finland	+11.7 Nov	+12.3 Nov	+4.0‡	0.77	0.83	0.5	3.76	4.11
Iceland	−1.9 Nov	−3.9 Q3	−13.3‡	68.4	63.1	2.1	15.01	na
Ireland	+35.3 Nov	−6.5 Q3	−4.8‡	0.77	0.83	0.4	3.78	4.09
Latvia	−4.7 Nov	−3.9 Nov	−14.1‡	0.54	0.58	−1.2	3.97	na
Lithuania	−5.0 Nov	−3.3 Nov	−9.5‡	2.66	2.85	−0.5	3.83	na
Luxembourg	−5.5 Oct	+4.8 Q3	na	0.77	0.83	−0.9	3.78	na
New Zealand	−3.9 Nov	+6.1 Q3	−8.5‡	1.45	1.46	4.1	6.70	6.01
Peru	+8.5 Nov	+1.8 Q3	+0.7	3.20	3.31	0.1	4.39	na
Philippines	−4.4 Nov	+4.4 Sep	+3.1	48.9	52.1	−0.8	5.56	na
Portugal	−23.1 Oct	−17.0 Nov	−7.9‡	0.77	0.83	−3.7	3.78	4.23
Slovakia	−3.5 Nov	−5.4 Sep	−5.8‡	26.9	30.8	−3.0	4.15	4.34
Slovenia	−2.0 Nov	−1.1 Nov	−2.1‡	0.77	0.83	−0.9	na	na

*Merchandise trade only. †*The Economist* poll. ‡Economist Intelligence Unit forecast. §Dollar-denominated bonds.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; JPMorgan; Bank Leumi le-Israel; Centre for Monitoring Indian Economy; Danske Bank; Hong Kong Monetary Authority; Standard Bank Group; UBS; Westpac.

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About sponsorship

Markets

Feb 1st 2007
From The Economist print edition

Markets

	Index Jan 31st	% change on one week	% change on Dec 30th 2005 in local currency	% change on Dec 30th 2005 in $ terms
United States (DJIA)	12,621.7	nil	+17.8	+17.8
United States (S&P 500)	1,438.2	–0.1	+15.2	+15.2
United States (NAScomp)	2,463.9	–0.1	+11.7	+11.7
Japan (Nikkei 225)	17,383.4	–0.7	+7.9	+5.3
Japan (Topix)	1,722.0	–1.0	+4.4	+1.8
China (SSEA)	2,927.8	–6.3	+139.8	+148.9
China (SSEB, $ terms)	160.7	–9.6	+149.6	+159.1
Britain (FTSE 100)	6,203.1	–1.8	+10.4	+25.9
Canada (S&P TSX)	13,034.1	+0.2	+15.6	+14.4
Euro area (FTSE Euro 100)	1,302.7	–0.2	+19.6	+31.8
Euro area (DJ STOXX 50)	4,178.5	–0.2	+16.8	+28.6
Austria (ATX)	4,522.0	+1.3	+23.3	+35.8
Belgium (Bel 20)	4,433.6	–0.7	+24.9	+37.6
France (CAC 40)	5,608.3	–0.5	+18.9	+31.0
Germany (DAX)*	6,789.1	+0.6	+25.5	+38.3
Greece (Athex Comp)	4,710.2	+0.3	+28.6	+41.6
Italy (S&P/MIB)	42,197.0	–0.9	+18.2	+30.2
Netherlands (AEX)	499.8	–1.3	+14.4	+26.1
Spain (Madrid SE)	1,612.1	+0.1	+39.4	+53.6
Czech Republic (PX)	1,663.4	+0.2	+12.9	+28.4
Denmark (OMXCB)	441.8	nil	+20.1	+32.4
Hungary (BUX)	24,059.4	–0.7	+15.8	+25.9
Norway (OSEAX)	523.4	+0.4	+38.9	+50.2
Poland (WIG)	54,558.2	+1.6	+53.2	+65.8
Russia (RTS, $ terms)	1,842.9	–1.0	+51.0	+63.7
Sweden (Aff.Gen)	376.7	+0.4	+28.4	+46.7
Switzerland (SMI)	9,135.1	–0.2	+20.5	+27.2
Turkey (ISE)	41,182.6	–2.0	+3.5	–0.9
Australia (All Ord.)	5,757.7	+0.1	+22.3	+29.6
Hong Kong (Hang Seng)	20,106.4	–3.4	+35.2	+34.2
India (BSE)	14,090.9	–0.1	+49.9	+52.8
Indonesia (JSX)	1,757.3	–2.7	+51.1	+63.4
Malaysia (KLSE)	1,189.4	+0.5	+32.2	+42.7
Pakistan (KSE)	11,272.3	+3.8	+18.0	+16.1
Singapore (STI)	3,125.6	–0.8	+33.2	+44.1
South Korea (KOSPI)	1,360.2	–1.7	–1.4	+5.9
Taiwan (TWI)	7,699.6	–3.0	+17.6	+17.3
Thailand (SET)	654.0	–0.5	–8.4	+8.1
Argentina (MERV)	2,070.6	nil	+34.2	+30.6
Brazil (BVSP)	44,641.0	–0.1	+33.4	+46.6
Chile (IGPA)	12,988.0	+0.3	+41.1	+32.7
Colombia (IGBC)	10,796.0	+0.5	+13.5	+15.1
Mexico (IPC)	27,561.5	+0.8	+54.8	+49.2
Venezuela (IBC)	43,965.9	+2.5	+115.6	+29.4
Egypt (Hermes)	58,220.0	–2.3	+5.2	+5.9
Israel (TA-100)	958.3	+0.3	+15.7	+25.2
Saudi Arabia (Tadawul)	7,041.2	+0.8	–57.9	–57.9
South Africa (JSE AS)	25,447.7	nil	+40.6	+23.0
Europe (FTSEurofirst 300)	1,514.7	–0.9	+18.7	+30.8
World, dev'd (MSCI)	1,500.2	–0.4	+19.3	+19.3
Emerging markets (MSCI)	901.5	–1.6	+27.6	+27.6
World, all (MSCI)	371.2	–0.5	+19.9	+19.9
World bonds (Citigroup)	649.4	–0.1	+4.7	+4.7
EMBI+ (JPMorgan)	405.5	–0.4	+10.0	+10.0
Hedge funds (HFRX)	1,293.0	nil	+10.7	+10.7
Volatility, US (VIX)	10.4	9.9	12.1	(levels)
CDSs, Eur (iTRAXX)†	21.5	+3.0	–41.5	–35.6
CDSs, N Am (CDX)†	27.9	+3.7	–39.6	–39.6
Carbon trading (EU ETS) €	2.31	–37.6	–89.1	–88.0

*Total return index. †Credit-default swap spreads, basis points.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac.

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Europe's dearest flats

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Monaco is the most expensive place in Europe to buy a flat. According to the Global Property Guide, a website aimed at people buying dwellings abroad, a 120 square-metre (1,292 square-foot) apartment in the principality will cost you almost €3m ($3.9m). London's swankiest districts (Belgravia, Chelsea and Knightsbridge) are in second spot—although monthly rents there are higher. The housing booms in Ireland and Spain have earned Dublin (€600,000) and Madrid (€480,000) places in the survey of the top dozen cities. The Baltic capitals of Vilnius (€455,000) and Riga (€362,400) are not far outside the top group. No German city makes our chart: the dearest is Munich, at €400,000.

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